FEDERAL TRADE COMMISSION DECISIONS

FINDINGS, OPINIONS, AND ORDERS

JANUARY 1, 1978 TO JUNE 30, 1978

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Appointed June 20, 1977

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FEDERAL TRADE COMMISSION DECISIONS

Findings, Opinions and Orders

IN THE MATTER OF

BOISE CASCADE CORPORATION, ET AL.

ORDER, OPINION, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket 8958. Complaint, April 18, 1974 — Final Order, Jan. 11, 1978

This order, among other things, requires a Boise, Idaho manufacturer and seller of softwood plywood, and four of its competitors, to cease, in connection with sales and transportation of their products, employing weight estimates to determine freight charges; and using any rate of freight other than that applicable to particular business transactions. The order further requires that respondents, when offering delivered prices, provide purchasers of their products the option of obtaining point of origin prices and furnishing their own transportation. Additionally, respondents must advise persons responsible for sales and policy of the terms of the order, and publish such terms, as prescribed.

Appearances

For the Commission: *James C. Egan, Jr., Amy R. Richter, Roger J. Leifer* and *Robert J. Enders.*

For the respondents: *Hammond E. Chaffetz, James H. Schink, Steven D. McCormack* and *Stephen C. Neal, Kirkland & Ellis,* Chicago, Illinois for Champion International Corporation, Georgia-Pacific Corporation, Weyerhaeuser Company and Willamette Industries, Inc. *John T. Loughlin, Robert T. Johnson, Jr.* and *Robert W. Sheppy, Bell, Boyd, Lloyd, Haddad & Burns,* Chicago, Illinois for Boise Cascade Corporation.

COMPLAINT

The Federal Trade Commission, having reason to believe that the above-named respondents have violated and are now violating Section 5 of the Federal Trade Commission Act (15 U.S.C. 45), and believing that a proceeding by it in respect thereof is in the public interest, hereby issues its complaint charging as follows:

PARAGRAPH 1. Respondent Boise Cascade Corporation is a corporation organized, existing and doing business under the laws of the State of Delaware with its principal office and place of business at Boise, Idaho. In 1971, Boise Cascade Corporation had sales of $1,785,870,000.

PAR. 2. Respondent Champion International Corporation is a corporation organized, existing and doing business under the laws of the State of New York with its principal office and place of business at 777 3rd Ave., New York, New York. In 1971, Champion International Corporation had sales of $1,599,829,000. [2]

PAR. 3. Respondent Georgia-Pacific Corporation (hereinafter "Georgia-Pacific") is a corporation organized, existing and doing business under the laws of the State of Georgia with its principal office and place of business at 900 S.W. 5th Ave., Portland, Oregon. In 1971, Georgia-Pacific had sales of $1,447,300,000.

PAR. 4. Respondent Weyerhaeuser Company is a corporation organized, existing and doing business under the laws of the State of Washington with its principal office and place of business at Tacoma, Washington. In 1971, Weyerhaeuser Company had annual sales of $1,299,533,000.

PAR. 5. Respondent Willamette Industries, Inc., is a corporation organized, existing and doing business under the laws of the State of Oregon with its principal office and place of business at 3800 1st National Bank Building, Portland, Oregon. In 1971, Willamette Industries, Inc., had sales of $194,173,636.

PAR. 6. Each of the respondents is substantially engaged in the manufacture, sale and distribution of softwood plywood. In the course and conduct of their business, each of the respondents is and has been for a substantial period of time engaged in selling such products to purchasers located in various States of the United States, and has caused such products to be transported from their facilities in various States of the United States to purchasers located in various other States of the United States. Each of the respondents is therefore engaged in "commerce," as "commerce" is defined in the Federal Trade Commission Act, and has been continuously so engaged for several years.

Definitions

PAR. 7. For the purpose of this complaint, the following definitions shall apply:

(a) "Softwood" – woods from coniferous trees such as pine, fir, spruce, and hemlock, which are generally light in texture, non-resistant and easily worked. [3]

(b) "Softwood plywood" (sometimes referred to as "plywood" in this complaint) – material consisting of sheets of softwood glued or cemented together with the grains of adjacent layers arranged at right angles or at a wide angle usually being made of uniformly thin veneer sheets on either side of a thicker central layer.

(c) "Phantom freight" – the differential in amount between the actual freight costs incurred in shipping a product and higher freight charges used as the basis for billing the customer.

Nature of Trade and Commerce

PAR. 8. The manufacture and sale of softwood plywood is a substantial and expanding industry in the United States. In 1971, domestic shipments were $1,246,911,000. Softwood plywood is a material which enters heavily into the cost of construction of residential and commercial buildings. There has been a trend toward factory-built housing in which 29 percent - 39 percent more plywood is used than in conventional housing. Large markets for softwood plywood include the major urban areas and suburban centers in the northeast and northcentral regions of the nation and certain urban areas in the South and the West.

PAR. 9. Historically, plywood was made from Douglas-fir trees and manufactured almost entirely in the coastal areas of the Pacific Northwest. In more recent years, the industry expanded to inland areas as types of softwood other than Douglas-fir began to be used in the manufacture of plywood. As a result of the development of new laminating techniques permitting utilization of the woods of southern pine, Georgia-Pacific established the first plywood mill in the South in Fordyce, Arkansas in 1963. Most of the large western plywood manufacturers thereafter established plants in the South. All of the respondents now have softwood plywood plants in the South.

PAR. 10. By the end of 1971, there were 51 softwood plywood plants located in the South. Since 1963, there has been a significant increase in the production of softwood plywood nationally, with most of the increase occurring in the South. By the end of 1971, production of plywood in the South reached approximately one quarter of total U.S. output. [4]

PAR. 11. In 1969, the top eight softwood plywood producers accounted for approximately 64 percent of domestic plant shipments and the top four producers accounted for approximately 48 percent of shipments. The concentration level has increased since that time. The 1969 concentration level increased from 1963 when the top four and top eight softwood plywood producers had approximately 36 percent and 50 percent of domestic plant shipments, respectively.

PAR. 12. In 1971, the top eight softwood plywood producers accounted for approximately 74 percent of southern production and the top four producers accounted for approximately 61 percent of that production. A number of plants have recently been built in the South by the leading producers and this has resulted in an increase in concentration in the South. The respondents are among the leading producers in either the nation or in the South.

Pacific Northwest Single Basing Point

PAR. 13. Before Georgia-Pacific opened its first softwood plywood plant in the South, respondents were charging softwood plywood delivered prices based upon rail freight rates computed from Portland, Oregon. Georgia-Pacific and each of the respondents which subsequently opened plants in the South have continued to charge delivered prices for softwood plywood computed on the basis of rail freight from the Pacific Northwest, despite substantial shipments of softwood plywood from respondent's plants located in the South and other places geographically distant from the Pacific Northwest. As part of this basing point system, respondents have refused to permit customers the option of purchasing softwood plywood at the plant at f.o.b. prices which did not include freight from the Pacific Northwest or to allow their customers to arrange for the mode of transportation cheapest to the customer.

PAR. 14. The parallel conduct of respondents and others in adhering to delivered prices based upon rail rates from the Pacific Northwest for shipments from mills located in other areas of the country has resulted in substantial margins of phantom freight accruing to respondents, particularly for shipments from plants in the South made to customers located in the southern, eastern, and northcentral areas of the [5] country. This conduct enables those respondents which have plants in the West to ship plywood from their western plants to customers in the East without being undercut in price by southern mills which have a substantial geographic cost advantage. An example of the extent of phantom freight involved in the basing point system is as follows:

> In September 1972, a retail dealer in New Orleans, Louisiana, purchased softwood plywood produced at a plant located 60 miles away in Holden, Louisiana. The dealer paid a delivered price of $4,289, which was computed on the basis of rail freight from Portland, Oregon. Portland is 2500 miles away and the freight was $764. The supplying plant in fact shipped the plywood to the purchaser by truck at a freight charge of $80. Approximately 16% or $684 of the purchaser's total delivered price consisted of phantom freight.

PAR. 15. The American Plywood Association, 1119 A St., Tacoma, Washington, to which most of the respondents belong, has disseminated to the industry freight books specifying appropriate rail rates from the Pacific Northwest. This has facilitated the workings of the above-described basing point system.

PAR. 16. The respondents and the rest of the industry use uniform estimated weights to quote delivered prices to customers. Inaccuracies in a number of these weights further inflate the amount of phantom freight.

Nature of the Offense

PAR. 17. In the conduct of the aforesaid business, the respondents individually, and in combination with other companies, are now using and for a number of years have used and pursued parallel courses of business behavior constituting unfair methods of competition and unfair and deceptive acts in commerce. Among the unfair methods of competition and the unfair and deceptive acts and practices which respondents individually, and in combination, have been and are now engaged are the following: [6]

(a) establishing and maintaining a system of delivered prices based on computation of rail freight from the Pacific Northwest for shipments made from mills located outside of that region;

(b) establishing and maintaining a system of delivered prices based on computation of rail freight and applying it to shipments made by other and cheaper modes of transportation;

(c) refusing to permit customers who purchase from southern plants the option of picking up purchases at the plant at true f.o.b. mill prices; and

(d) using identical and inaccurate estimated weights as basis for quoting delivered prices.

Effects

PAR. 18. The capacity, tendency and effects of the conduct of respondents hereinbefore alleged are, among others, to:

(a) stabilize prices and provide certainty in the pricing of softwood plywood among competitors;

(b) reduce and hinder actual and potential competition among respondents in the sale and distribution of softwood plywood;

(c) create disincentives to the most efficient location of producing points;

(d) create disincentives to customers to locate close to producing points;

(e) discourage use of the cheapest and most efficient mode of transportation in given cases;

(f) discriminate in prices between customers; and [7]

(g) mislead and deceive customers with respect to freight.

PAR. 19. The conduct of respondents hereinbefore alleged were and are unfair methods of competition, and unfair or deceptive acts in commerce in violation of Section 5 of the Federal Trade Commission Act (15 U.S.C. 45), as amended.

INITIAL DECISION BY MORTON NEEDELMAN, ADMINISTRATIVE LAW JUDGE

NOVEMBER 29, 1976

[2] I

STATEMENT OF THE CASE

The complaint in this proceeding issued on April 18, 1974. It charges that respondents, manufacturers of softwood plywood, have, individually, and in combination, pursued parallel courses of business behavior constituting unfair methods of competition, and unfair and deceptive acts and practices in violation of Section 5 of the Federal Trade Commission Act (15 U.S.C. 45).

Specifically the complaint alleges that respondents, individually and in combination, have: (a) established and maintained a system of delivered prices for plywood[1] which is based on computation of the freight charge from the Pacific Northwest for shipments made from mills located in the South; (b) established and maintained a system of delivered prices based on computation of rail freight and applied these computations to shipments made by other and cheaper modes of transportation; (c) refused to permit customers the option of purchasing at respondents' southern plywood plants at a true F.O.B. price; and (d) used identical and inaccurate estimated weights as the basis for delivered price quotes. (Complaint ¶'s 17(a)-(d)).

The complaint further alleges that the effects of these practices have been to: stabilize prices and provide certainty in the pricing of plywood among competitors; reduce and hinder actual and potential competition among respondents in the sale and distribution of plywood; create disincentives to the most efficient location of plywood producing points; create [3] disincentives for customers to locate close to plywood producing points; discourage use of the cheapest and most efficient mode of transporting plywood; discriminate in prices between customers; and to mislead and deceive customers with respect to freight. (Complaint ¶'s 18(a)-(b)).

Respondents' answers, filed by Boise Cascade on May 22, 1974 and by the others on June 7, 1974, admit certain corporate and jurisdictional facts, but deny all substantive allegations in the complaint.

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[1] Unless otherwise specified, the term "plywood" as used in this initial decision means softwood plywood only. The terms "western plywood," "Douglas fir plywood," and "fir plywood" are used interchangeably. I have also used interchangeably the terms "southern plywood," "yellow pine plywood," and "pine plywood."

In the prehearing stage, complaint counsel had extensive discovery of respondents' records. Upon completion of the discovery phase, the case-in-chief began on December 2, 1975, and was concluded on December 22, 1975. The defense case was presented between January 19, 1976, and April 1, 1976. The rebuttal and surrebuttal cases were heard between April 19 and June 8, 1976. During these hearings, all counsel were afforded full opportunity to be heard, and to examine and cross-examine witnesses.

The record was closed on June 30, 1976, for the receipt of evidence. Proposed findings of fact and conclusions of law, together with briefs were filed by the parties on July 30, 1976. Answering briefs were filed on August 30, 1976. Oral argument on the briefs was heard on September 8, 1976. On September 7, 1976, complaint counsel moved to strike from the record certain documentary exhibits which had not been relied on either in proposed findings or in replies. This motion was opposed in part by respondents, and except for those deletions which respondents were against, complaint counsel's motion was granted by my order dated September 13, 1976. By leave of the Commission, the date for filing this initial decision was set for November 29, 1976. [4]

After reviewing all the evidence, the proposed findings, conclusions, and briefs submitted by the parties, and based on the entire record, including my observation of the demeanor of all witnesses, I make the following findings of fact.[2]

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[2] Proposed findings not adopted in the form proposed or in substance, are rejected as either not supported by the entire record, or as involving immaterial matters.

The following abbreviations are used in citing to the record: "Tr." (transcript of testimony); "CX" (complaint counsel's exhibits); "RX" (respondents' exhibits). CX 1, an index to complaint counsel's exhibits, contains a description of each document, date received or rejected, source, and part of the document which is in evidence. (Exhibits which were offered and received for only a part of the document, indicate received portion bracketed in red.) The same information for respondents' exhibits appears on RX 1.

All *in camera* exhibits are listed in my omnibus *in camera* order of June 23, 1976. By the terms of this order (¶ 4) there is no limitation whatever on the public use of this material in decisions written by the undersigned, the Commission, or other reviewing authorities. Also, my *in camera* order of June 23, 1976 (¶ 5) states that *in camera* status will end on June 30, 1981, when all *in camera* exhibits are to be placed on the public record.

In reviewing documentary exhibits, it is helpful to consult CX's 801A–805E which give the employment history of senders and recipients of respondents' memoranda and letters. [5]

The record, excluding pre-hearing conferences, consists of 4,703 pages (121 of which are oral argument on briefs). There are approximately 1,000 trial exhibits consisting of several thousand pages. The witnesses were as follows:

Name	*Called By*	*Tr. Pages*
Robert E. Smith C.C. Crow Publications, Inc.	Complaint Counsel ("c.c.")	314–367 535–569
Lester E. Anderson Random Lengths Publications, Inc.	c.c.	368–527
Gordon J. King Hampton Lumber Sales (formerly with Boise Cascade)	c.c.	570–702
James C. Schmidt Louisiana Pacific Corporation (formerly with Boise Cascade		

(Continued)

(Fn 2. Continued)

and Georgia-Pacific)	c.c.	703-802
William R. Coston Oregon-Pacific Company (formerly with Champion)	c.c.	804-913
Donald K. Barton (formerly with Georgia-Pacific)	c.c.	914-981
George W. Rummel Gulfgate State Bank (formerly with Champion)	c.c.	991-1045 [6]
James F. Lynn MacMillan-Bloedel Corporation	c.c.	1056-1108
Mahlon W. Day National Building Centers (formerly with Weyerhaeuser)	c.c.	1131-1205
Michael Glassman Federal Trade Commission	c.c.	1215A-1287
Frank V. Langfitt Georgia-Pacific	Resp.	1370-1563
Stanley S. Dennison Georgia-Pacific	Resp.	1566-1734
William Swindells, Jr. Willamette	Resp.	1737-1874
Paul A. MacDonnell Georgia-Pacific	Resp.	1879-1984
Robert A. Starling Georgia-Pacific	Resp.	1997-2080
Daniel I. Allred Georgia-Pacific	Resp.	2083-2184
R. Paul Kay Weyerhaeuser	Resp.	2193-2318
Donald W. Cobb Boise Cascade	Resp.	2392-2452 [7]
Craig Marshall Boise Cascade	Resp.	2456-2520
Conrad R. Kelley Champion	Resp.	2561-2756
Bob Prange Bowie-Sims-Prange	Resp.	2759-2859
David Vagos Furman Lumber Company	Resp.	2862-2915
Milton Sandy, Jr. Sandy Lumber Sales Company	Resp.	2920-2949
John P. O'Reilly Haggerty Lumber and Supply Company	Resp.	2958-2975
Robert L. Fallow, Jr. Roseburg Lumber Company (formerly with Boise Cascade)	Resp.	2981-3031
Roy Weinstein National Economic Research Associates	Resp.	3065-3260 3263-3460 3464-3579
Peter O. Steiner The University of Michigan	Resp.	3587-3825 4433-4566
Robert E. Ridgeway American Plywood Association	c.c.	4047-4154
Gilbert N. Miller Georgia-Pacific	Resp.	4201-4388

[8] II

FINDINGS OF FACT

The Respondents

1. Respondent Georgia-Pacific Corporation ("Georgia-Pacific") is a Georgia corporation with its principal office and place of business located at 900 S.W. Fifth Ave., Portland, Oregon. (Complaint and Georgia-Pacific Answer ¶ 3.)

2. Georgia-Pacific is a manufacturer and distributor of softwood and hardwood plywood, paper and other forest products. In 1971, Georgia-Pacific's total corporate sales were $1,447,300,000. (Complaint and Georgia-Pacific Answer ¶ 3; CX 460.)

3. Respondent Champion International ("Champion") is a New York corporation. At the time complaint issued its principal office and place of business were located at 777 3rd Ave., New York, New York. (Complaint and Champion Answer ¶ 2.) Champion's corporate headquarters was subsequently moved to Stamford, Connecticut. (Tr. 2570.)

4. Champion (through its United States Plywood Division) is a manufacturer and distributor of plywood and other wood products. (Tr. 2561.) Champion's 1971 sales of all products were $1,599,829,000. (Complaint and Champion Answer ¶ 2.)

5. Respondent Boise Cascade Corporation ("Boise") is a Delaware corporation with its principal office and place of business located in Boise, Idaho. (Complaint and Boise Answer ¶ 1.)

6. Boise manufactures and distributes wood products, including plywood,[3] and had total sales [9] in 1971 from all products of $1,785,870,000. (Complaint and Boise Answer ¶ 1.)

7. Respondent Weyerhaeuser Company yellow is a State of Washington corporation with its principal office and place of business located in Tacoma, Washington. (Complaint and Weyerhaeuser Answer ¶ 4.)

8. Weyerhaeuser is a manufacturer and distributor of plywood and other forest products, including lumber, particleboard, wallboard, and paper. In 1971, Weyerhaeuser's sales of all products were $1,299,533,000. (Complaint and Weyerhaeuser Answer ¶ 4; CX's 101H–i, 110E, 807B.)

9. Respondent Willamette Industries, Inc. ("Willamette") is an Oregon corporation, with its principal office and place of business located at 3800 1st National Bank Building, Portland, Oregon. (Complaint and Willamette Answer ¶ 5.)

10. Willamette is a manufacturer and distributor of paper products, plywood, lumber, and particleboard. In 1971, Willamette's total

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[3] In addition, Boise's Eastern Division produces "Kingsberry" pre-fabricated homes which are manufactured in panelized sections and assembled on site. (CX 421, p. 9.)

sales from all products were $194,173,636. (Complaint and Willamette Answer ¶ 5; CX 65B.)

The Product

11. This case involves plywood manufactured by respondents from two types of softwood evergreen trees — the Douglas fir grown principally in or near the Pacific Northwest, and the yellow pine grown in the South.[4] **[10]**

12. Plywood is a flat wood panel, constructed of thin sheets of wood bonded together with the grain direction of each sheet or "ply" at right angles to the one adjacent to it. The plywood "sandwich" consists of thin outer veneer sheets on either side of a thicker central layer. (CX 320, p. 2; Tr. 572, 1374, 1895.)

13. Plywood is manufactured by debarking and cutting logs into "peeler blocks" approximately 8 feet 6 inches in length. The peeler blocks are softened by steaming. (Tr. 1373.)[5]

14. After the steaming process, the "peeler blocks" are then revolved against a sharp blade and "peeled" into continuous sheets in much the same manner as paper is unwound from a roll. (Tr. 1373–74.)[6] These peeled veneer sheets are passed down a conveyor, clipped to the desired lengths and dried. (CX 320, pp. 2–3, 11–12; Tr. 1374.)

15. The veneer sheets are then graded by quality according to the incidence of defects. The highest grades, designated "N" (intended for natural finish) and "A," must be completely smooth and devoid of any open defects when sanded. The remaining grades — "B," "C," and "D" — may have defects of specified size and in some instances of specified number. Grade "D" veneer **[11]** may have any number of defects so long as these defects do not seriously impair the strength or serviceability of the panel. (CX 320, pp. 2–3, 11–12; Tr. 386–87, 1894–95.)

16. The veneers are coated with glue and arranged together in the desired number of plies — most plywood is made in 3, 4, or 5 plies — to form the plywood "sandwich." The stacked veneers are then glued under pressure in a hot press. (CX 320, p. 2; Tr. 572, 1374.)

17. Plywood panels with inner cores composed of D grade veneers are known as "interior type." Interior grade panels are not used in

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[4] "Southern yellow pine" is not one species. It is a term applied to Loblolly, Slash, Shortleaf, and Longleaf pines. (CX 320, p. 4.)

[5] The technical standard for the manufacture of plywood is established by the plywood industry under the auspices of the Product Standards Section of the U.S. Department of Commerce and is published by the National Bureau of Standards in "Softwood Plywood - Construction and Industrial Standard PS 1-66," and its successor, PS 1-74. (CX 320; Tr. 1895.)

[6] Because it is impossible to peel the log entirely, there is always a small "core block" remaining after the peeler block is converted into veneers. These cores constitute a by-product of the plywood production process and are either sold outright or ground into chips and then sold. (CX 901B *in camera;* Tr. 4209.)

applications where there is constant exposure to weather. Plywood panels of "exterior type" construction, which may be exposed to weather, are constructed with C grade inner veneers. (CX 320, pp. 2–3; Tr. 350.)[7]

18. Following the drying process the plywood panels are trimmed to desired size. Panels 4 feet by 8 feet are the most commonly produced. (RX's 434A–435F; Tr. 350, 1374.)

19. Plywood panels containing higher veneer grades are often sanded to meet the requirements of such specialized end-uses as interior cabinet work and stair treads. In addition, panels may be improved or upgraded by repairs (patches) which eliminate defects in the face veneers. (CX 320, pp. 11–12, 20; Tr. 1374.) Plywood which incorporates the N, A or B grades of veneer on the face panel and which is fully sanded for complete smoothness on both sides is known as "sanded" plywood. (CX 320, p. 11.)

20. Unsanded plywood — also known as "sheathing" — contains C and D grades of veneer in the face and back. Since plywood grade designation is expressed by reference to the face and back veneers, sheathing designated as **[12]** "CD interior" consists of C grade veneer on the face, D grade veneer on the back and D grade inner plies. (CX 320, p. 11; Tr. 353, 1895–96.)

21. In addition to the sanded and sheathing products,[8] plywood veneers of various grades may be manufactured into specialty products designed for particular uses. Among these are special engineering grades designed for applications in which unusually rigid structural properties are important. (CX 320, p. 20.)

22. Of the 12.5 billion square feet of plywood shipments reported by the American Plywood Association in 1974, approximately 8.7 billion square feet, or 69.7 percent, were sheathing; 2.7 billion square feet (21.9 percent) were sanded; and 1 billion square feet (8.3 percent) were specialty products. The most commonly produced softwood plywood product is CD interior with exterior glue,[9] which accounted for approximately 66.6 percent of sheathing shipments reported by the American Plywood Association in 1974. (RX's 11N, Q.)

23. Residential construction in which CD sheathing is widely used for flooring, walls, and roofing,[10] is the principal plywood application. The American Plywood Association estimates that 54.8 percent of

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[7] Almost all plywood — western or southern, interior or exterior — is now made with a moisture repellant exterior glue line. (Tr. 361.)

[8] "Plyform" or "concrete form" is a plywood product which has an oiled edge and is used to form the mold for poured concrete. After the concrete hardens, the plyform is removed and used again. (Tr. 353, 536.)

[9] Also known as "Standard Exterior" or "CDX." Note that CDX is an "interior"-type panel bonded with an exterior glue. (Tr. 360–61, 1894–96.)

[10] Plywood has taken over almost all of the roof-sheathing market, and is an important factor in sidewall sheathing as well as in flooring where it is replacing the traditional oak floor. (Tr. 1375.)

industry production in 1973 was used in residential construction. [13] Other construction accounted for 13.6 percent. The industrial market including such applications as packaging materials and furniture accounted for 18.6 percent. The agricultural and over-the-counter markets accounted for 13 percent of industry production. (RX 12G; Tr. 353, 1374–75, 1423.)[11]

The Industry

24. The production and sale of plywood is a substantial industry. In 1964 there were 164 plywood mills producing 11,678,621 thousand square feet (3/8 inch basis).[12] In 1974 the number increased to 195 mills which produced 15,878,380 thousand square feet (3/8 inch basis). (RX 11E.)

25. From the origin of the plywood industry in the early twentieth century until 1947, all plywood was produced in the States of Washington and Oregon. In 1947 the western plywood industry expanded into northern California, and in 1952 to the States of Idaho and Montana. (RX's 11E–F.) [14]

26. During the early 1960's, the technology of laminating southern pine veneers into a successful plywood bond was developed. The first southern mill specifically designed for plywood was constructed by Georgia-Pacific at Fordyce, Arkansas,[13] and the first shipment of plywood from that mill was made in December 1963. (CX 460; p. 10; Tr. 1377–78.) Before the lamination problem was solved, southern pine was mainly used in the manufacture of pulp, paper or lumber, but it was not used for plywood. (RX 90B.)

27. Today there are three major plywood producing regions in the United States: the original "western" region encompassing the States of Oregon and Washington west of the Cascade mountains and

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[11] These end-use percentages have remained relatively constant during the time period 1971–73:

	1971	*1972*	*1973*
Residential construction	53.6%	54.6%	54.8%
General construction	12.8	12.8	13.6
Industrial	19.5	19.2	18.6
Agriculture/over-the-counter	14.0	13.4	13.0

(RX 12G)

[12] For statistical purposes, various thicknesses of plywood are frequently converted to a uniform 3/8 inch basis for measuring volume in square feet regardless of thickness. For example, a 4 foot x 8 foot panel of 1/2 inch plywood contains 32 square feet (4 feet x 8 feet) of surface footage on an actual basis and 42.7 square feet [1/2 inch divided by 3/8 inch (4 feet x 8 feet)] of surface footage on a 3/8 inch basis.

[13] During 1962 and 1963, Georgia-Pacific acquired the Crossett Company in Crossett, Arkansas and the nearby Fordyce Lumber Company. With these acquisitions, which together cost about $140 million, Georgia-Pacific obtained 800,000 acres of pine timber. (RX 90B.)

northern California; the "inland" (or "Inland Empire") region, which includes those portions of Washington and Oregon east of the Cascade mountains, and the States of Idaho and Montana; and the "southern" region comprising Maryland, Virginia, North Carolina, South Carolina, Georgia, Florida, Alabama, Mississippi, Arkansas, Louisiana, Texas, and Oklahoma. (RX 11C.) The production share by region in 1974 was as follows:

Western	61.4%
Southern	32.3
Inland	6.3

(RX 11D)

In terms of the key product manufactured in the South, plywood sheathing, the regional shares in 1974 were as follows:

Southern	45.7%
Western	35.6
Inland	18.7

(RX 11Q)

[15] 28. Total industry and respondents' production of all softwood plywood are as follows:

TABLE 1: Production of *All* Plywood By Industry and By Individual Respondents

(In thousands of square feet - 3/8 inch basis)

	1964	*1969*	*1971*	*1973*
Industry	11,678,621	13,694,392	16,634,971	18,304,599
Georgia-Pacific	1,038,000	1,944,000	2,709,000	2,434,000
*Boise	401,985	920,419	1,366,648	1,352,480
Weyerhaeuser	624,280	851,600	1,036,700	1,213,200
*Champion	763,683	1,046,125	1,134,717	1,200,600
*Willamette	510,463	811,434	1,001,523	1,074,800

(Source: CX 930C)

* Includes all production of joint venture mills in which the particular respondent is a joint venture partner.

29. The five respondents account for the following percentage of total industry production:

TABLE 2: Percentage of Total Production Controlled By Each Respondent

	1964	*1969*	*1971*	*1973*
Georgia-Pacific	8.89	14.20	16.28	13.30
*Boise	3.44	6.72	8.22	7.39

Weyerhaeuser	5.35	6.22	6.23	6.63
*Champion	6.54	7.64	6.82	6.56
*Willamette	4.37	5.93	6.02	5.87
5 firm total	28.59	40.70	43.57	39.74

(Source: Finding 28)

* Includes all production of joint venture mills in which the particular respondent is a joint venture partner.

[16] 30. Total industry and respondents' production of southern pine plywood are as follows:

TABLE 3: Total Softwood Plywood Production By Industry And By Respondents

(In thousands of square feet - 3/8 inch basis)

	1964	*1969*	*1971*	*1973*
Industry	80,024	2,875,355	4,410,062	5,558,618
Georgia-Pacific	64,000	962,000	1,729,000	1,824,000
*Boise	0	52,802	66,202	123,447
Weyerhaeuser	0	196,000	310,100	472,600
*Champion	0	189,041	264,037	265,481
*Willamette	0	157,650	280,696	328,407

(Source: CX 930C)

* Includes all production of joint venture mills in which the particular respondent is a joint venture partner.

31. The five respondents account for the following percentage of total southern plywood production:

TABLE 4: Percentage of Total Southern Production Controlled By Each Respondent

	1964	*1969*	*1971*	*1973*
Georgia-Pacific	79.98	33.46	39.21	32.81
*Boise	0	1.84	1.50	2.22
Weyerhaeuser	0	6.82	7.03	8.50
*Champion	0	6.57	5.99	4.78
*Willamette	0	5.48	6.36	5.91
5 firm total	79.98	54.17	60.09	54.22

(Source: Finding 30)

* Includes all production of joint venture mills in which the particular respondent is a joint venture partner.

[17] 32. The record does not contain precise proof of the dollar value of annual plywood production, but it can be estimated. In 1973, Georgia-Pacific, the dominant southern plywood producer, had an average sales realization of approximately $100 (per thousand square feet) on sales from its southern sheathing plants. (RX 452 *in camera.*) Applying the Georgia-Pacific experience to total southern production (which is predominantly sheathing), this would mean industry-wide

sales of southern sheathing of $555,861,800. Western production is more difficult to estimate because the product mix of the western and inland regions is varied and includes higher priced items such as sanded and specialty. In any event, since southern production was only 30 percent of total industry production in 1973 (CX 321, p. 3), it can readily be seen that total industry production (18,304,599 thousand feet) produced sales of approximately $2 billion. Census data, which combines softwood plywood with veneers, show 1972 sales valued at $2,011,500,000. (CX's 677A–E.)

33. Georgia-Pacific is the largest manufacturer of softwood plywood, and it is recognized by other softwood plywood manufacturers, including respondents, as the industry leader and the dominant southern plywood producer. (CX's 110Z9, 325B, 356A, 461, p. 47, 502A, 589, 616; RX 90A–B.)

Respondents' Plywood Operations

34. With the exception of respondent Willamette,[14] which for all practical purposes has no distribution outlets apart from its mills, respondents operate multiple level distribution systems where sales are made either directly from producing mills through centralized mill sales offices (usually in carload lots or from owned and operated and geographically dispersed distribution outlets variously called "distribution centers," "branches," "warehouses," "CSC's" ("Customer Service Centers," [18] Weyerhaeuser's name for its outlets) or "BM & S's" ("Building Materials and Service," Boise's name for its outlets). (See Findings 35–58.)

These distribution outlets may make sales out of inventory in "break-bulk" quantities or may sell on the basis that the plywood is to be shipped directly from the mill in carload or truckload lots, referred to as a "direct mill" sale by a branch. Customers of both the mills or the distribution outlets may range across the entire spectrum of plywood customers from end-users such as residential and industrial contractors and manufacturers to intermediate buying groups, retail lumberyards, and the distribution outlets of other plywood producers. But essentially, respondents' distribution outlets are wholesale warehouses which sell to lumber dealers who, in turn, resell to building contractors. (CX's 356A, 461, p. 48; Tr. 995–96, 1133–34).

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[14] Almost all of Willamette's sales are made from its mills: only 2 percent of its sales are made from company-owned retail lumberyards located in Oregon. (See Finding 55.)

Georgia-Pacific

35. In 1975 Georgia-Pacific produced plywood at 18 mills located as follows:

West

Coos Bay, Ore.
Coquille, Ore.
Springfield, Ore.
Toledo, Ore.

South

Crossett, Ark. (2 mills)
Emporia, Va.
Fordyce, Ark.
Gloster, Miss.
Louisville, Miss.
Monticello, Ga.
Russellville, S. C.
Savannah, Ga.
Taylorsville, Miss.
[19] Whiteville, N. C.
Talladega, Ala.
Warm Springs, Ga.
Prosperity, S. C.[15]

(CX's 452; Tr. 1529–30)

36. Georgia-Pacific's Building Products Division initially markets all of Georgia-Pacific's softwood plywood (whether produced at Georgia-Pacific mills in the West or South or purchased from other producers) through sales departments located in Portland, Oregon; Crossett, Arkansas; and Augusta, Georgia. The Crossett and Augusta sales departments are under the control of the Portland sales office. About 90 percent of Building Products Division sales of plywood are made to Georgia-Pacific's own Distribution Division. (CX 133A; Tr. 1427, 1570.)

37. In addition to its own production, Georgia-Pacific purchases plywood from several sources including both manufacturers and independent wholesalers. (Tr. 2087.) Virtually all of the plywood purchased from outside sources is sold by the Georgia-Pacific

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[15] A Georgia-Pacific mill in Chiefland, Florida was closed during 1974. Three mills (Urania, Louisiana; New Waverly, Texas; and Corrigan, Texas) were spun off in 1972 to Louisiana-Pacific Corporation pursuant to an order of the Federal Trade Commission. (CX's 453A–B, 461; Tr. 1530.)

Distribution Division. (Tr. 1561–62.) Plywood purchased from outside sources accounts for approximately 25 percent of the plywood sold by Georgia-Pacific's Distribution Division.[16]

38. Georgia-Pacific's Distribution Division has 145 "Distribution Centers" operating throughout the United States. The centers or branches are wholly-owned outlets which sell a full line of wood and other building material products to dealers, industrial accounts, and [20] major contractors. Each of these centers is operated as an individual profit center which means that plywood produced at company mills or outside sources is transferred or sold at a certain cost and the centers are responsible for making a profit on the resale. (CX 461, p. 48; Tr. 954, 1560–61, 1566–68, 1891, 2000, 4383; see also Findings 97, 98.)

39. As indicated in Finding 36, more than 90 percent of Georgia-Pacific's plywood sales are made through the branches. The remainder is made directly from the mills through "Product Managers" located in Portland, Oregon; Crossett, Arkansas; and Augusta, Georgia. (Tr. 1372–73, 1427, 1483–85, 1569–70.)[17]

Boise

40. Boise began producing softwood plywood in 1959. (Tr. 2334.) Presently, it owns and operates 13 softwood plywood mills, located as follows:

West

Kettle Falls, Wash.
Yakima, Wash.
Spokane, Wash.
Camp Adair, Ore.
Valsetz, Ore.
Albany, Ore.
Independence, Ore.
Medford, Ore.
Sweet Home, Ore.
Elgin, Ore.
Emmett, Idaho

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[16] Only 1 1/2 percent of total sales of southern plywood are derived from the sale of outside purchases. (Tr. 1549–50.)

[17] In addition, there are mill representatives located in Atlanta, Georgia; Clifton, New Jersey; Washington, D. C.; Chicago, Illinois; and Dallas, Texas. (Tr. 1483–85.)

[21] *South*[18]

Moncure, N. C.
DeQuincy, La.[19]

(CX's 315A–C *in camera*, 363C *in camera*, 401; Tr. 573, 2334)

41. A Boise subsidiary, Bovill, Inc., is a 50 percent joint venture partner with a Southern Natural Gas Company subsidiary, Southern Natural Resources, Inc., in Boise Southern Company ("Boise Southern"). Boise Southern operates the softwood plywood mill located in DeQuincy, Louisiana, which began production in 1972. (CX's 316, 317 *in camera*, 421, p. 20, 682A–Z67 *in camera;* Tr. 2393.)

For the purpose of this litigation, and specifically in ruling on the admissibility of certain Boise Southern exhibits, I have concluded that evidence relating to the acts and practices of Boise Southern in connection with the operation of the DeQuincy mill may be received in evidence as indicative of the policies of respondent Boise for the following reasons:

[22] First, the joint venture agreement between Boise and Southern Natural Gas contemplates that respondent Boise will contribute its lumber expertise to the joint venture. Southern Natural Gas had no expertise in this area. (CX's 682M–N, S–U *in camera.*)

Second, by the terms of the joint venture agreement respondent Boise may appoint or remove the chief executive officer of Boise Southern at will. (CX's 682G–i *in camera.*) This indicates latent control over the policies of Boise Southern.

Third, key operating personnel have transferred freely between Boise Southern and respondent Boise. For example, the current president of Boise Southern (Bill Patterson) had previously worked for Boise (CX 802K) and Jerry Johnson, the plywood sales manager at Boise Southern, was initially employed by Boise and later returned to work for Boise. (Tr. 2412–13, 2451.) A Boise official testified: "before the [DeQuincy] mill started operating and before he [Johnson] moved down there we instructed him on procedures of selling down there." (Tr. 2412.) While he was employed at DeQuincy Mr. Johnson conferred with a plywood sales control manager at Boise several times a week. (Tr. 2413–14.) Weekly market reports prepared by Mr. Johnson at Boise Southern, which included pricing, production, and shipment information, were sent to officials at Boise. (CX's 370, 802A–P.) Moreover, while he was in the employ of Boise Southern, Mr. Johnson received a copy of the Moncure weekly market report which contained pricing, production and shipment information, as well as a copy of the Boise quarterly plywood price forecast. (CX's 383, 389, 840A–D.)

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[18] In addition to the southern mills indicated, Boise acquired a plywood plant in Pensacola, Florida in December 1969. This plant was permanently closed in October 1974 and the equipment was removed. Its primary products throughout its years of operation were hardwood plywood, hardwood plywood paneling, and hardwood plywood siding made from woods such as mahogany, cypress, and cativo. It produced small amounts of softwood plywood between 1972 and 1974. (CX 315A *in camera;* Tr. 575, 669, 2352–57.) Still another Boise plywood mill located at Fort Bragg, California was sold in 1973. (CX 401.)

[19] See Finding 41 for ownership and control of the DeQuincy, Louisiana mill.

Finally, the Boise Southern profit statement indicates that Boise has the responsibility for selling the softwood plywood produced by Boise Southern (CX 350F *in camera*), but apparently Boise's actual role in marketing has been advisory. (Tr. 2413.) [23]

42. Boise's Building Materials and Services Division ("BM & S") currently operates 44 outlets which sell a variety of wood and hardware products, including softwood plywood. Each of these "BM & S" outlets is a profit center. (CX's 318A–C, 319, 421, p. 9; Tr. 596–97, 738.)

43. Western softwood plywood produced by Boise and *not* sold through "BM & S's" is sold by the Boise Wood Products Division located in Portland, Oregon. Southern softwood plywood is essentially sold by Boise directly from its mill sales office located in Moncure, North Carolina. (Tr. 2333, 2381–82.)[20] In addition, some of Moncure's plywood production has been sold by the six Boise "BM & S's" located in Springfield, and Newport News, Virginia; Georgetown, Delaware; and Raleigh, Charlotte and Greensboro, North Carolina. (CX's 387A–B; Tr. 2389, 2478–80.) Boise Southern (the joint venture with Southern Natural Gas) sells southern softwood plywood directly from its mill sales office in DeQuincy, Louisiana. (Tr. 2393–94.)

Weyerhaeuser

44. Weyerhaeuser produces softwood plywood at 12 mills located as follows:

West

Longview, Wash.
Snoqualmie Falls, Wash.
Coos Bay, Ore.
Cottage Grove, Ore.
Klamath Falls, Ore.
Springfield, Ore.

[24] *South*

Dierks, Ark.

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[20] Until mid-1970, southern pine plywood produced at Moncure was sold by Boise's Portland, Oregon sales office. (Tr. 576, 671, 2381.)

Jacksonville, N. C.
Mountain Pine, Ark.
Philadelphia, Miss.
Plymouth, N. C.
Wright City, Okla.

(CX 167; Tr. 2198)

45. Weyerhaeuser sells over 50 percent of its plywood through direct carload and truckload facilities ("trading centers") located in Tacoma, Washington and Hot Springs, Arkansas. (Tr. 2194–95.)

46. The balance of Weyerhaeuser's domestic plywood sales (about 32 percent of production) are made through 62 wholly-owned distribution outlets, known as Customer Service Centers ("CSC's") located throughout the United States.[21] (Tr. 2194–95, 2244.) Weyerhaeuser's "CSC's" are warehouses which receive direct carloads and resell in smaller quantities. (Tr. 2194, 2199.)

47. The Weyerhaeuser "CSC's" are individual profit centers. (CX's 881A–B; Tr. 1166.) The profit of a "CSC" is calculated by subtracting from its gross sales, the transfer cost of the wood sold and the costs of operation. (Tr. 1166–68, 1170.)

48. In addition to the distribution of its own production, Weyerhaeuser annually purchases for resale approximately 500 million square feet of plywood from other manufacturers. (Tr. 2244–45.) Approximately 90 percent of the sales of this outside plywood are made through the Weyerhaeuser "CSC's." (Tr. 2245.) [25]

49. Weyerhaeuser, through its "CSC's" and trading centers, sells mainly to retail dealers (RX's 434B, D, H) including chains such as Lowe's (RX 434i; Tr. 2286) and Wickes (Tr. 2284) as well as some independent wholesalers and wholesale buying organizations. (CX 112; RX 434C; Tr. 2284.)

Champion

50. Champion, through its U.S. Plywood Division, produces plywood at 14 mills which are located as follows:

West

Shasta, Calif.
Seattle, Wash.
Mapleton, Ore.
Willamina, Ore.

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[21] If Weyerhaeuser's outside purchases of plywood (500 million feet or 1/3 of total sales) are included, the "CSC's" sell about 51 percent of all plywood produced or purchased by Weyerhaeuser. (Tr. 2245.)

Gold Beach, Ore.
Lebanon, Ore.
Roseburg, Ore.
Bonner, Mont.

South

Hammond, La.
Waycross, Ga.
Newberry, S. C.
Corrigan, Texas
Cordova, Ala.
Pocomoke City, Md. (50% interest)

(Tr. 2565, 2743–44, 2944)

51. Virtually all of the plywood produced by Champion mills or purchased from outside sources is sold by wholly-owned company warehouses or branches. Champion owns 125 warehouses located throughout the United States. Each of these branches operates as an independent profit center. (Tr. 813–14, 1022–23, 2569–72, 2698.) The branches sell a full line of wood products, primarily to retail dealers and to the building and industrial markets. (Tr. 2569–72.) [26]

52. The Champion branches order softwood plywood through Champion's central purchasing office, located in Eugene, Oregon, and known as West Coast Purchasing (WCP). Plywood is ordered by the branch either for direct shipment to the customer or for its own inventory for subsequent distribution to customers, usually by truck. (Tr. 2572–73.)

53. Approximately 60 percent of total Champion sales are made out of branch inventory while about 40 percent of total sales are made directly from the mill. Mill sales are usually in carload or truckload quantity. Sales shipped directly from the mill to the branch's customer, save the branch the transactional cost of breaking bulk and putting the plywood into inventory. Accordingly, branches try to sell as much plywood as they can directly from the mill. (Tr. 814, 2572.)

Willamette

54. Willamette owns and operates 11 softwood plywood mills located as follows:

West

Sweet Home, Ore.
Dallas, Ore.

Foster, Ore.
Lebanon, Ore.
Griggs, Ore.
Springfield, Ore.
Redmond, Ore. (50% owned)

South

Dodson, La.
Natchitaches, La. (50% owned)
Ruston, La. (85% owned)
Minden, La. (50% owned)

(CX's 39A, 65B; Tr. 1738–39)

[27] 55. Approximately 98 percent of the plywood produced by Willamette is sold directly from its various mills. Most sales are made by telephone out of offices located in Albany, Oregon and Ruston, Louisiana. Only about 2 percent of Willamette's production is sold through seven wholly-owned retail lumberyards located in Oregon. (Tr. 1740–41.)

56. Virtually all products sold through Willamette's Albany and Ruston sales offices, as well as the sales by its wholly-owned retail lumberyards, are manufactured by Willamette. (Tr. 1743.)

57. Willamette's principal plywood customers at the mill level are office wholesalers (those who ordinarily buy and sell without taking physical possession of the plywood) and wholesale distributors (those wholesalers who ordinarily take possession of the plywood before reselling it), although mill direct sales are also made to retail lumberyards and industrial accounts such as fabricators. (CX's 87C, i.) From its wholly-owned retail lumberyards, Willamette sells primarily to building contractors and to do-it-yourself consumers. (Tr. 1740.)

"Commerce"

58. Each respondent manufactures, sells, and distributes softwood plywood throughout the United States, and each is engaged in "commerce" as "commerce" is defined in the Federal Trade Commission Act. (Complaint and Answers ¶ 6.)

Significance of Price

59. Competition in the southern plywood industry is essentially in terms of price since pine sheathing, the primary item produced by

respondents and other southern producers, is considered to be fungible and not readily susceptible to quality differentiation. (Tr. 1896, 2603.)[22]

[28] 60. The demand for plywood sheathing is mainly a function of the residential housing industry. (RX's 11H, 12D, 13i, 14A; Tr. 675, 1423, 1966.) Overall demand for the product does not increase by reason of a price reduction at a time of depressed housing starts. (RX's 10G, 69M, Z9.) On the other hand, prices increase sharply when the number of housing starts accelerate. (Tr. 1423 and see note 98, *infra.*) There are long-term contracts for the sale of plywood, but in those instances the price is left open to be decided at time of shipment. (See Finding 94.) Generally plywood is bought by the housing industry at time of actual need. (RX's 10G–H, 11D, 13C, i, 14A–16B.) These ultimate purchasers do not build up inventories.[23]

Because of the price inelastic nature of the product, a price reduction does not produce an overall increase in demand; it merely means that the existing business, as determined by the housing market, will be shared at a lower profit among the producers. Given the nature of the demand for the product, and the concentrated structure of the industry (Finding 31), plywood producers have a strong incentive to avoid price cutting. As a Georgia-Pacific branch manager put it:

> If all of a sudden I am starting, or I feel that I am getting more than my share of that market, it is an indication to me that maybe I am selling my wood too cheap. (Tr. 1892–93; see also Tr. 1758–59, 2742.)

Or in the words of a Willamette official who was giving his version of why West Coast freight was added to southern pine plywood prices to arrive at a delivered price which was near the western price: [29]

> He [the plywood purchaser] couldn't buy plywood any cheaper from anyone else so there was no reason to cut our prices. (Tr. 1754.)

Respondents' Pricing Practices

61. The central issue in this case is the legality of the pricing practices followed by respondents since 1963 after the opening of the southern pine plywood industry.

62. As indicated earlier (Findings 25, 26), prior to the opening of the southern plywood industry in 1963 by Georgia-Pacific, virtually all[24] plywood was manufactured from the Douglas fir trees grown in

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[22] For evidence of quality differences between southern and western plywood see Findings 131(a), (b).

[23] Purchases for inventory, however, may be made by lumber wholesalers and retailers in anticipation of rising markets. (Tr. 849.) But see CX 356A which indicates that independent distributors are becoming increasingly "less willing to stock [plywood]. . .for redistribution" and Tr. 2871 for evidence that retailers do not tend to buy for future needs.

[24] Plywood had been manufactured in the South prior to Georgia-Pacific's entry, but Georgia-Pacific was the first producer to build a southern plant designed exclusively for plywood manufacture. (Tr. 1876–77.)

the Pacific Northwest and the "Inland Empire" areas of Idaho and Montana.

63. All softwood plywood, whether produced in the West or the South, is generally bought on a delivered price basis. (CX 665D; Tr. 321, 956–57, 1084, 1148–49, 1911, 2340.)[25]

64. Both before and after the opening of the southern plywood industry in 1963, the delivered price of western plywood was a function of a mill price to which actual freight from the West Coast was added. (Tr. 1391–92, 1747, 1863.)[26] In the sale of western plywood, the **[30]** freight charge, which was paid by the purchaser to the carrier, was the actual rail rate from the West Coast to the customer's destination.[27]

65. The reason Georgia-Pacific was anxious to expand into plywood production in the South was that it had found that southern pine plywood for rough uses, such as sheathing for residential construction, costs no more to produce than its Douglas fir counterpart, and Georgia-Pacific expected that in the long run it would cost less. The main advantage however which Georgia-Pacific anticipated from the opening of the southern plywood industry was in the area of freight. In 1965 it cost buyers $15 to $18 to ship 1,000 square feet of plywood from the Pacific coast to southeastern cities such as Memphis and Atlanta. Actual freight costs from southern pine plywood mills, even allowing for slightly heavier weight per square foot, ranged from a third of that amount to practically nothing depending on mill and customer location. By pricing its southern pine plywood at or near the same *delivered* price of Douglas fir plywood, Georgia-Pacific planned to add this saving in freight to its gross margins. (RX's 90A–B.)[28] **[31]**

66. There were several possible impediments to Georgia-Pacific's plan. In the first place, the mere fact that plywood was to be shipped from the South could add materially to price uncertainty in the industry and thereby reduce margins. This particular hazard came about because of the crucial differences between western and southern freight rates. (Findings 67, 68.)

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[25] For different forms of delivered pricing in the South, see Finding 126.

[26] While the freight charge is based on the actual rail rate from the West Coast, the total amount paid may be overstated because the rate is multiplied by "association" weights rather than the actual weight of a particular shipment. See Finding 85.

[27] Except for inland (Idaho and Montana) mills which use the West Coast rate. (See note 30, *infra.*)

[28] In 1963, Georgia-Pacific projected an annual return on investment before taxes of 59.7 percent from a Crossett, Arkansas plywood mill and a net profit before taxes of $14.93 (per thousand square feet on average sales of $57.75). (CX's 845A–C *in camera.*) In 1964, Georgia-Pacific projected a return on investment after taxes of 27.5 percent from a second Crossett, Arkansas mill and a capital recovery period of about three years. From this mill Georgia-Pacific projected an average net profit before taxes of $23.90 (per thousand square feet) on average net sales of $66.75 (per thousand square feet). (CX's 488A–B, F.) A basic assumption of the planning for this Crossett mill was that there would be a freight "advantage" (*i.e.*, difference between West Coast and actual freight) of $8.75 per thousand square feet. An even greater "advantage" ($15) was projected from a Virginia plywood mill. (CX 490B.) For similar calculations for Louisville, Mississippi ($12) see CX 491F; for a Moncks Corner, South Carolina plant ($12.00) see CX 493C; for Waverly, Virginia ($15.00) see CX 493E; for Savannah, Georgia ($12.50) see CX 495D; and for Chiefland, Florida ($12.50) see CX 501D.

67. The Interstate Commerce Commission rail rates applicable to *western* plywood shipments are established in the form of concentric bands or zones running north and south and originating with the Portland, Oregon zone which includes most of the western plywood producing region. As a shipment of plywood travels from the West to the East, it enters progressively higher West Coast freight zones and the rail rate is commensurately higher.[29] Almost all plywood shipments originating in the zone of origin where the Douglas fir plywood mills are located have the same freight rate (the so-called "Portland, Oregon" rate) to any point within one of the [32] eastern destination zones.[30] Under this "zone" freight rate for western plywood, there is no uncertainty about the freight rate factor in delivered prices. A customer located in Greensboro, North Carolina, for example, pays the same freight rate regardless of the mill in Oregon or Washington from which the plywood originated. Similarly, that precise same freight rate is applicable to customers located anywhere in the freight band stretching from Maine to Florida along the East Coast of the United States. (CX's 51A–B, 348A, 681; Tr. 579, 1391–92, 1445–46, 1745, 1932–34, 2806.)

68. In contrast to the predictable West Coast freight rate, the Interstate Commerce Commission plywood freight rates from points of origin in the southern United States are established on a "point-to-point" basis; that is, the published freight rate for each point of origin varies to each point of destination. For example, the rail rate from Ruston, Louisiana, to Greensboro, North Carolina, is significantly different from the rate from Ruston to Griffith, North Carolina, and still other freight rates apply to shipments from Minden, Louisiana to either Greensboro or Griffith, North Carolina. (CX's 51B, 91Z32, 865; Tr. 374, 510, 1391–93, 2741.)[31]

[33] 69. In addition to the problem of the southern freight rate, there were other factors which could have created uncertainty in the new southern plywood venture, and thereby depress prices. Thus as southern plywood output grew, it was anticipated that pressure would

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[29] Rail freight rates for plywood are ordinarily expressed as dollars and cents per 100 pounds. (Tr. 1933.) Plywood prices are ordinarily expressed as dollars and cents per 1,000 square feet. For pricing purposes, the weight of 1,000 square feet of 1/2 inch plywood is 1,525 pounds (an "association" weight, see Finding 84) and the freight charge to the "$2.79" zone will be $2.79 (per hundred pounds) times 1,575 pounds (per thousand square feet), or $42.55 per 1,000 square feet.

[30] There is a separate West Coast freight schedule for plywood shipped into the southwest United States from mills located in northern California. (CX's 348A, 681; Tr. 999–1000.) Although mills located in Idaho and Montana, as well as mills located in eastern Washington and Oregon, are not in the West Coast (*i.e.*, the Portland, Oregon) zone, it is common industry practice to use the higher West Coast rate in calculating delivered prices from these "inland" mills. (CX 348A and Tr. 2626–27.)

[31] In addition, while western freight rates are applied uniformly to the total weight in a car, southern freight rates are based on an "incentive" system, which means that there is a lower freight rate per 100 pounds as the total weight in the car increases. (Tr. 1393, 1785–86.)

be created for producers to share at least some of the freight savings with their customers. (RX's 90A–B.)[32]

70. Also, Georgia-Pacific's planning for the opening of the southern pine industry contemplated that the southern production would add no more to the available supply than "about 10 percent of the normal annual growth in the industry" and —

> Since no let-up is in sight and since the market research people have projected a long-range substantial growth in the industry, there would seem to be no problem from this standpoint. (CX 488C.)

Clearly a "problem" would exist (in the form of a threat of sharply lower prices) if as the new southern production came on stream, instead of "normal annual growth" there existed a severely depressed housing market.[33]

[34] 71. Finally, there was concern that instability in southern prices and any tendency of southern production to depress plywood prices in general, would have an adverse impact on major producers of Douglas fir plywood in the Pacific Northwest. (RX's 90A–B.)

72. Against the background of a plan to add the difference between West Coast and actual freight to its gross margins, and the possible creation of price instability because of factors inherent in the southern venture, Georgia-Pacific adopted a policy at the opening of the southern pine plywood industry in 1963 of including in the delivered price for southern yellow pine plywood, freight calculated on the basis of the West Coast rail freight rate from Portland, Oregon, rather than the actual freight from its southern mills. (RX's 90A–B; Tr. 1391–95.) In other words, a West Coast freight factor was used to arrive at prices for pine plywood which were intended to be the same as the delivered prices of fir plywood. (Tr. 1431, 1634–35.) Georgia-Pacific's policy of including West Coast freight in Southern plywood delivered prices has continued since 1963. (Findings 75(a), 76(a), 78(a), 96(a).)

73. Georgia-Pacific's policy of calculating delivered prices by adding West Coast freight was followed by the other respondents when they subsequently entered the southern pine plywood industry. The record shows the following:

(a) *Willamette.* Willamette began producing southern pine plywood in 1965 at the Ruston, Louisiana mill of its Santiam Lumber Company subsidiary. (CX 1A; Tr. 1750–51.) With its entry into the southern plywood industry, Willamette told its customers that "These prices [southern pine plywood prices] are based on the current Coast mill less 5 & 3% with freight from the Coast added." (CX's 2B, 5A, 12A.) Willamette has added West Coast freight to its southern plywood prices ever since. [35] (CX's 3, 5A–C, 6A–B, 7, 9A–15A, 16–17C, 18, 20, 22–25, 68, 69A, 88A–L, 89A, 90, 861, 862A, 884H; see also Findings 76(e), 78(d), 79(d).)

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[32] See also CX 490C where calculations were made by Georgia-Pacific in 1964 on the difference between maintaining and losing the "freight advantage." Note that in 1971, Georgia-Pacific personnel are concerned about a customer ". . .trying to find out about any freight advantage that might be enjoyed by Southern Pine sheathing producers." (CX 584, see also CX 585.)

[33] At about the same time that Georgia-Pacific was making its projections, Weyerhaeuser anticipated that the production of the southern mills could have created a severe competitive problem in the form of a price depressant unless housing starts increased. (CX's 99W; see also Tr. 2210–11.) This fear of the southern plywood industry persists: in September, 1974, a Boise Southern official reported "there is not enough demand to use all that is produced." (CX 417.)

(b) *Weyerhaeuser*. Weyerhaeuser began producing southern pine plywood in 1964 and 1965 at mills located in Jacksonville and Plymouth, North Carolina. (CX 99C; Tr. 2199.) Weyerhaeuser entered the southern yellow pine industry with the expectation that the delivered prices of its southern mills would approximate the delivered prices of West Coast plywood, with the difference between actual and West Coast freight "to be an incremental gain for the [southern] mill." (CX 99V(1); Tr. 2216.) Thereafter, Weyerhaeuser continued to add West Coast freight to the price of its southern pine plywood. (CX's 97, 98, 104A, 106A, 107A, 108, 111A, 112B, 113B, 114A, 130A, 137A, 883A, 885–87; see also Findings 75(b), 76(c), 78(c), 96(c).)

(c) *Champion*. U.S. Plywood (Champion's plywood division) entered the southern pine plywood industry in 1964 as a 50% partner with Temple Industries in a joint venture called "Southern Pine Plywood Corporation" of Diboll, Texas. (Tr. 2609.)[34] From the outset of its southern plywood business, it was U.S. Plywood's policy to sell pine plywood at a price equal to the price of Douglas fir delivered from the West Coast. (Tr. 2610.) Champion has added West Coast freight to its southern plywood prices ever since. (CX's 192A, 200, 202A–B, 203A, 205B, 219B, 238A–B, 266, [36] 271H, J, 362A–C; Tr. 811, 1016; see also Findings 75(c), 76(d), 78(e), 96(d).)

(d) *Boise*. Boise's initial investment in the southern plywood industry was in the form of the purchase of a minority interest in the Triangle Plywood Corporation, Moncure, North Carolina, in 1968. Boise acquired a majority interest in this mill in 1969 and 100% ownership in 1973. (CX 364D *in camera;* Tr. 2335.) Boise planned for its entry into the southern pine plywood industry on the basis of the freight advantage between West Coast and southern rates. (CX's 324A–J.) With its entry into the southern plywood business, Boise used West Coast freight in calculating delivered prices. (Tr. 578–79, 717, 757.) For current use by Boise of West Coast freight, see Findings 76(b), 78(b), 96(b).)

74. The southern pine plywood prices of respondents and all other southern plywood producers,[35] include West Coast freight, whether the transaction is in the [37] form of contract or spot sales, or made from distribution centers or from mills, and irrespective of the "form" in

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[34] By 1967, in addition to its joint venture at Diboll, Texas, U.S. Plywood had a wholly-owned plywood mill located in Hammond, Louisiana, and a joint venture plywood mill in Pocomoke City, Maryland. (Tr. 2727.)

[35] The only important exception to this pattern is the practice of one non-respondent producer, MacMillan-Bloedel, of quoting an F.O.B. price plus actual freight. (Tr. 1058–60.) However, even in the case of MacMillan-Bloedel the West Coast freight is absorbed into the quoted F.O.B. price. (CX's 202A–B, 417.)

Subsequent to issuance of the proposed complaint in this matter, Georgia-Pacific changed, at least temporarily, to an F.O.B. mill form of pricing southern pine plywood. That change remained in effect for approximately two months. (CX's 631A, 642, 661, 808A, 809A–810B; Tr. 1408–09, 1667–68.) Georgia-Pacific's F.O.B. mill price was not a bona fide mill price, however, since it was calculated on the basis of West Coast freight. (CX 631A.) Georgia-Pacific has reverted to pricing southern pine plywood (both for internal transfers and for sales to outside customers) on the basis of a "mill price" to which West Coast freight is added. (Tr. 1539.) Also, in September, 1974, a Boise official reported that a number of mills in Georgia and Alabama (not otherwise identified) had gone to an F.O.B. mill price plus actual freight. (CX 417; see also Tr. 739–40, 866.) In February 1974, Willamette contemplated using a true F.O.B. mill price and discontinuing the practice of quoting on a West Coast basis in order "to give a clearer, more concise price to our customer while preventing us from making mistakes as to where we can get the best price and still give our customer the most competitive price." (CX 68.)

which the price may be quoted. (Findings 75–80, 125, 126.) Moreover, the West Coast freight factor is included in intra-corporate transfers, which means that it is passed on to dealers, builders, and eventually to the consuming public. (Findings 75–80, 96–98.)

75. In sales of southern plywood from respondents' distribution outlets, the record shows the following about the use of West Coast freight:

(a) *Georgia-Pacific*. The Georgia-Pacific distribution centers include West Coast freight in setting prices to their customers. (CX's 610A–i, 867–69; Tr. 919, 931, 934, 956–57.)[36]

[38] (b) *Weyerhaeuser*. In order to determine the "CSC" selling price for southern pine plywood, West Coast freight "must be added" to a base price. (CX's 104A, 106A, 107A, 108, 111A, 114A.)

(c) *Champion*. West Coast freight is added to a base price in arriving at the delivered price which the U.S. Plywood branches charge their customers. (CX's 238A, B, 263, 266, 271H, J; Tr. 810–11, 1016.) In addition, West Coast rail freight is added in sales by branches which are shipped directly from the U.S. Plywood mills to the customers of the branch. (CX's 232–37, 239A-251A; Tr. 814, 1026–27.)

76. In contracts for the sale of southern plywood, the record shows the following with respect to the use of a West Coast freight factor:

(a) *Georgia-Pacific*. In 1969 50% of Georgia-Pacific's southern pine sheathing sales in the southeast were made pursuant to contracts. The 1969 contracts, as well as later Georgia-Pacific contracts, included West Coast freight in the prices. (CX's 366A, B, 531, 586G.)

(b) *Boise*. West Coast freight is part of the delivered price in contracts negotiated at the Moncure mill. (Tr. 719–20, 3000.)

(c) *Weyerhaeuser*. In all contracts for the sale of southern pine plywood, West Coast rail freight is added by Weyerhaeuser. (Tr. 1190–92.)

(d) *Champion*. Approximately 15% of the total softwood plywood sales of U.S. Plywood branches is sold pursuant to [39] long-term contracts. (Tr. 2654.) In Champion's long-term contracts for the sale of southern plywood West Coast freight is added. (CX's 194–196, 205A–B, 209A–B, 215A–B, 216A–B.)

(e) *Willamette*. As much as 40% of Willamette's southern production has been sold pursuant to contracts. (Tr. 1845–47.) These contracts include West Coast freight. (CX 90; Tr. 1838.)

77. In intra-corporate transfers of southern plywood between respondents' mills and respondents' distribution outlets, West Coast freight is added. (See Finding 96.)

78. In sales of southern plywood from respondents' mills, the record shows the following with respect to use of West Coast freight:

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[36] See also CX 590 which shows that a Georgia-Pacific branch sets its price "based on Crow's." As indicated in Finding 91, the *Crow's* price always requires the automatic addition of West Coast freight.

(a) *Georgia-Pacific.* In sales of southern pine plywood made directly by Georgia-Pacific's mills, West Coast freight is added. (CX's 581, 880; Tr. 712, 739–40.)[37]

(b) *Boise.* In sales from the DeQuincy mills, the Boise Southern policy is —

> We sell our wood on a net delivered price to destination. To figure this price you take your base price less a 5–3 discount and add the West Coast freight. (CX 417; see also CX 35A, F *in camera.*)

For Boise's policy respecting use of West Coast freight in sales of plywood produced by its Moncure, North Carolina mill, see Finding 93(b) and Tr. 578–79.[38]

(c) *Weyerhaeuser.* In direct mill sales of southern pine plywood by Weyerhaeuser, West Coast freight is added. (CX's 885–87; Tr. 1186.)

(d) *Willamette.* Since Willamette began selling southern pine plywood, its mills have computed their delivered prices by adding on the West Coast rail freight rate to base prices. (CX's 2A–B, 3, 5A–C, 6A–B, 7, 9A–15A, 16–17C, 18, 20, 22–25, 68, 69A, 88A–L, 89A, 90, 861, 862A, 866A.)

(e) *Champion.* In its direct mill sales, U.S. Plywood adds West Coast freight to a base price. (Tr. 814, 863–64, 1026–27; see also Tr. 2132, 2724.)

79. In inter-manufacturer sales and purchases of southern plywood between respondents, or between respondents and other manufacturers, the record shows the following about the use of West Coast freight:

(a) *Georgia-Pacific.* In purchases of southern pine plywood by Georgia-Pacific, West Coast freight is added to a mill price. (CX's 360A-C, 601A-B, 609A-B, 628A-B; Tr. 1551.)

(b) *Boise.* In Boise's purchases of southern pine plywood for its Kingsberry Homes Division (a manufacturer of panelized homes), West Coast freight is added to [41] arrive at the delivered price. (CX's 336A–C, 353, 361, 362A–C, 366A–B, 397, 405.)

(c) *Champion.* The West Coast rail rate is used in purchases by U.S. Plywood from other southern mills. (CX's 199A–B, 595A–C, 664.)

(d) *Weyerhaeuser.* In purchases of southern plywood by Weyerhaeuser from Willamette, a base price is used which requires that West Coast freight be added. (CX's 41, 58, 884H.)

80. Although a substantial proportion of southern plywood is shipped to buyers by truck, the West Coast *rail* rate is used by respondents to arrive at delivered prices, whether shipments are made by rail *or* truck. (CX's 15A, 75C, 76E–F, 88D, 89A, 158P–Z15, 238A–B, 253B, 254, 255, 263, 401, 440A, D, L, S, 441A, E, i, K–L, 442A, G, N, S, X, Z3, Z7, Z8, 581, 596A–C, 702B; RX's 347A–E; Tr. 579, 1536.)[39]

81. Southern plywood is invoiced either freight prepaid or freight collect with the delivered price calculated to include West Coast

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[37] See also CX 549 which shows that sales by mills are treated in the same manner as mill direct sales by branches. In mill direct sales by branches, West Coast freight is added. (See Finding 97.)

[38] Until it was closed in 1974, Boise's Pensacola, Florida mill included West Coast freight in sales of southern plywood. (CX's 355W *in camera*, 360A–C.)

[39] See Findings 120–122 for respondents' policies respecting truck pick-ups by customers.

freight. In terms of net return to the seller or payments by the buyer, there is no difference between a transaction invoiced freight collect or freight prepaid. If freight is prepaid, the mill pays the actual freight to the carrier and receives from the buyer the total invoiced delivered price including West Coast freight. If the terms of the transaction are freight collect, the buyer deducts the amount of actual freight, pays it to the carrier, and remits the balance of the delivered price, which includes West Coast freight, to the seller. [42]

I attach no significance to the fact that most southern pine plywood is invoiced on a freight prepaid basis while most western plywood is invoiced freight collect.[40] Complaint counsel failed to prove, as alleged in Complaint ¶ 18(g), that there is any deception in the sale of southern plywood whether it is sold freight prepaid or freight collect. Purchasers of plywood know that the delivered price includes West Coast freight, and there is no evidence that respondents intend to conceal (or have concealed) the West Coast freight factor by invoicing on a freight prepaid basis. (See Tr. 2240–41, 2804.)

West Coast Freight Formula and Price Uncertainty

82. By using the West Coast freight factor, respondents have transferred the certainty of the western freight rate schedule to the South. As a result the freight factor in the price of southern pine plywood does not vary by mill or customer location.[41] The freight is calculated as if all the southern mills were located in the Portland, Oregon zone, and as if all customers were located in one of the neatly concentric (and predictable) West Coast zones where the rates increase as plywood is shipped from the West to the East. (CX 51A-B; see also Tr. 374, 713, 1402, 1525, 2741.)

83. Uncertainty about other aspects of southern plywood prices was also limited by practices followed by respondents. One of these practices relates to the fact that the freight charge on a particular transaction involving either western or southern plywood is a function of the West Coast rate multiplied by the weight of the plywood. Because the weight of plywood may vary from mill to mill (depending in part on the particular [43] species of softwood used in the manufacturing process), this factor, too, could have caused price uncertainty. (CX's 471, 808C, 864; Tr. 1828–29, 2723.)

84. The problem of weight uncertainty has been resolved by use of the so-called "association" weight of plywood rather than the actual weight of each shipment. The "association" weights (CX's 192A, 470A;

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[40] See CX's 69A, 126A, 863A, 866A, 886Z29; Tr. 1830, 2240; but see also Tr. 880, 1657 for evidence of a contrary practice (freight collect shipments from southern mills) by several respondents.

[41] See, however, Finding 142 which discusses certain "add-ons" to customers located in non-primary areas.

Tr. 357–58, 394–95, 815) are also known in the industry as "estimated," "standard," "shipping," "guaranteed,"[42] "established," "average," or "industry" weights. (Tr. 357–58, 395, 587, 1063, 1537, 2722–23.) There is a different "association" weight for each thickness, to wit:

Thickness (Inches)	*"Association" Weight Per Thousand Pounds*
1/4	790
5/16	950
3/8	1125
1/2	1525
5/8	1825
3/4	2225

(CX's 17B, 604)[43]

[44] 85. The "association" weights are usually above the actual weights of western plywood resulting in "underweights" which always accrue to the benefit of respondents' mills. (CX's 32A, 36B–D, 37A, 40A–B, 191B, 192A–B, 213, 325A–B, 365Z11 *in camera,* 423A, C–F, H, J, L, N, P *in camera,* 424A–429B *in camera,* 430A, C, E, G–H, *in camera,* 431A–C *in camera,* 432A, C, E, G *in camera,* 433A *in camera,* 434E *in camera,* 435A, C–J *in camera,* 436D *in camera,* 437E *in camera,* 438 *in camera,* 439D *in camera,* 473A–484D *in camera;* Tr. 595, 815–16, 2239–40.)[44] Southern pine weighs more than Douglas fir; therefore, the actual weights of southern plywood are closer to the "association" weights. (CX 192A; Tr. 815, 1066, 2242, 2476–77.) Nevertheless, there are "underweights" in the southern plywood industry. See, for example, CX's 471, 559K which indicate underweights at most Georgia-Pacific southern plywood mills and CX 864 which shows that all Willamette southern mills have had underweights on an annual basis; but see also CX 192A ("there really are no underweights, as a rule, on southern pine").

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[42] A U.S. Plywood official believed that the term "association" weights implies "that someone got together and decided on a set of weights for all plywood shipped. The fact that many other mills use the same shipping weights we do is purely coincidental." Accordingly, this official advised his sales personnel "Please make certain that all of your people who handle plywood sales are aware of the importance to always refer to shipping weights as 'Guaranteed Weights'." (CX 193.)

[43] The "association" weights currently in use in the plywood industry were contained in the National Recovery Act Code of Fair Competition, published in 1934. (RX's 8D, 9D.) The same weights were subsequently published by the Office of War Information in 1943 (RX's 6A, 7F), and by the Office of Price Stabilization in 1952. (RX 5F.) The use by the Douglas fir plywood industry of such a weight schedule was erroneously thought to have been discontinued prior to a Commission challenge to the legality of the practice in *Douglas Fir Plywood Association,* 47 F.T.C. 416, 440 (1950) *rev'd sub. nom. Oregon-Washington Plywood Co.* v. *FTC,* 194 F.2d 48 (9th Cir. 1952).

[44] For evidence that respondents' marketing strategy (shipment of lightest wood to distant markets) is directed at maximizing "underweights," see CX's 323, 377C *in camera,* 499A. Additional evidence respecting the preservation of "underweights" is shown in CX's 54, 192A, 213.

86. While the use of association weights in the South may not result in the same volume of "underweight" profit as that produced in the West, such an industry-wide schedule is essential in order to reduce price uncertainty, and, in fact, it has resulted in freight charges which are absolutely predictable. (Finding 88.) Aside from its [45] role in assuring such certainty in freight charges, industry-wide "association" weights serve no apparent legitimate purpose. Thus an official of Georgia-Pacific observed that actual average weights for each mill can be calculated and this "would be beneficial to both the railroad industry and Georgia-Pacific." (CX 472A; see also CX 485B and Tr. 1541.) One producer, MacMillan-Bloedel, on the basis of actual tests, has established with the railroads a schedule containing an approved weight for each thickness of plywood which is substantially different from the "association" weight. (Tr. 1064–65.)

87. Respondents use "association" weights in arriving at the total West Coast freight charge, whether the sale of southern plywood is made from a distribution center or mill, and whether it is a spot or a contract sale.[45] In addition, "association" weights are used in all intra-corporate transfers. The record evidence showing the use of "association" weights appears as follows:

(a) *Georgia-Pacific*. Georgia-Pacific's sales of southern softwood plywood, including intra-corporate transfers, are made on the basis of freight charges calculated from "association" weights.[46] (CX's 487B, D, 516A–C, 544A–E, 559K, 591B, 594B, 597D, 604, 617B, 618B, 620B, 623B.)

(b) *Boise*. Boise calculates freight charges for southern plywood on the basis of "association" weights. (CX's 387A–388C; Tr. 587, 590–91, 2382, 2390.)

(c) *Weyerhaeuser*. At all times since Weyerhaeuser has sold southern softwood plywood, it has computed the freight charges [46] on the basis of association weights. (CX's 97, 98, 111A, 114A; Tr. 1164–66, 1190, 2239.)

(d) *Willamette*. Willamette uses "association" weights in calculating freight charges in its mill sales. (CX's 17A–B, 51B, 69A, 88D; Tr. 1828.)

(e) *Champion*. U.S. Plywood uses "association" weights in its computation of freight charges. (CX's 192A–B, 238A–B, 282A–G, 284A–D, 362B; Tr. 2722–23.)

88. The combination of the West Coast rail freight rate and "association" weights eliminates all uncertainty about the freight factor in the delivered price of southern plywood. The freight charge to any customer in any of the West Coast freight zones is completely predictable; in fact, no calculation is necessary since *Crow's* and *Random Lengths*, the industry's trade publications, conveniently multiply the West Coast rate by the "association" weights. For example, *Crow's* typically reports:

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[45] ". . .all shipments [of southern pine] are based on West Coast freight to destination, again using association or guaranteed weights. . . ." (CX 192A.)

[46] Except for the period when Georgia-Pacific experimented with F.O.B. mill prices. (CX's 808A–810B; see note 35, *supra*.)

PLYWOOD FREIGHT RATES[1]

	.46[2]	.50	.65	.83	1.34	1.45	1.53	1.60	1.63
790[3]	3.65	4.75	5.15	6.55	10.60	11.55	12.10	12.65	12.90
950	4.35	5.70	6.20	7.90	12.75	13.85	14.55	15.20	15.50
1125	5.20	6.75	7.30	9.35	15.10	16.45	17.20	18.00	18.35
1525	7.00	9.15	9.90	12.65	20.45	22.25	23.35	24.40	24.85
1825	8.40	10.95	11.85	15.15	24.45	26.65	27.90	29.20	29.75
2225	10.25	13.35	14.45	18.45	29.80	32.50	34.05	35.60	36.25

	1.65	1.67	1.70	1.72	1.80	1.84	1.91	1.93	1.97
790[3]	13.05	13.20	13.45	13.60	14.20	14.55	15.10	15.25	15.55
950	15.70	15.85	16.15	16.35	17.10	17.50	18.15	18.35	18.70
1125	18.55	18.80	19.15	19.35	20.25	20.70	21.50	21.[illegible]	22.15
1525	25.15	25.45	25.95	26.25	27.45	28.05	29.15	29.45	30.05
1825	30.10	30.50	31.05	31.40	32.85	33.60	34.85	35.20	35.95
2225	36.70	37.15	37.85	38.25	40.05	40.95	42.50	42.95	43.85

(CX 879B)[47]

[1] Plywood freight rates per thousand pounds as of January 29, 1971. Rates have increased substantially since that time. For example, the rate in the $1.97 zone has increased to $2.79 as of January 19, 1976. (Tr. 1392.)

[2] Rate in zones from West Coast to the East Coast.

[3] "Association" weights per thousand pounds.

[47] 89. Price uncertainty in the plywood industry is further reduced by the widespread use of prices published by *Crow's* and *Random Lengths* as the mill or base prices to which West Coast freight multiplied by "association" weights is added. (Findings 90–99.)

90. *Crow's*[48] and *Random Lengths*[49] are trade publications which report the prices for plywood and other wood products that prevailed in the market during the preceding week. Prices reported in these publications are based on a rotating sample of mills and wholesalers throughout the country. (Tr. 335–36, 340–41, 377–81, 383, 412, 414–15.) The prices reported in the two publications are considered by the publishers to be "judgment calls" and are representative prices at the time the publications go to press. (Tr. 343–44, 421–22.) Three of the respondents (Georgia-Pacific, Champion, and Willamette) have been

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[47] Tables such as the one appearing in CX 879B are known throughout the industry and are used daily by all plywood buyers and sellers. (Tr. 539.)

[48] Published by C.C. Crow Publications, Inc., Portland, Oregon. *"Crow's"* is used herein to refer to both *Crow's Plywood Letter* which has been published on Friday of each week since April 1958, as well as the *Mid Week Report* which first appeared in March 1974. (Tr. 315–16, 320–23, 325.)

[49] Published by Random Lengths Publications, Inc., Eugene, Oregon. *"Random Lengths"* is used herein to refer to a weekly *Price Guide and Market Report,* which has reported plywood prices since the late 1950's, as well as a Wednesday *Midweek Report* which first appeared in January 1974. (Tr. 368–71.)

asked regularly by these publications to report their prices, while two others (Boise and Weyerhaeuser) have been surveyed sporadically. (Tr. 336, 382, 413–14, 561.)

91. The prices quoted in *Crow's* and *Random Lengths* are in the form of a "mill" or "base"[50] price to which rail freight from the West Coast *must* be added, and the [48] standard industry wholesale discounts of 5 percent and 3 percent[51] are deducted, in order to arrive at delivered prices. This "mill" form is used by *Crow's* and *Random Lengths* in the reporting of both southern pine and western fir plywood prices. (CX 680A; Tr. 321, 334–35, 354, 374, [49] 376, 402–03.) The prices appearing in *Crow's* and *Random Lengths* are intended to be the prices charged by producing mills in sales to independent wholesalers or to company-owned distribution outlets: they do not purport to be the prices charged by wholesalers or distribution outlets in sales to retailers. (Tr. 418.)

92. The position of the respondents that there is no pattern of uniform price lists[52] in the plywood industry to which West Coast freight is added, vastly understates the importance of the two industry price reporters. The weight of the evidence is that in calculating offering prices, respondents routinely use *Crow's* or *Random Lengths* in arriving at their base prices.[53] Thus Champion's Southeast Regional Sales Manager observed:

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[50] In the case of southern pine plywood, the "mill" or "base" price should not be confused with a bona fide F.O.B. price since customers cannot pick up at the "mill" or "base" price and thereby avoid West Coast freight. (See Finding 120.) The buyer's delivered cost is the "mill" or "base" price plus an amount equal to West Coast freight which is automatically added; or when a mill pick up is made by the buyer, he pays the delivered price including West Coast freight, less a small discount. (Finding 121.) In the case of western plywood, the *Crow's* or *Random Lengths* prices are an F.O.B. price in the sense that actual freight (except for inland mills) is added to obtain delivered cost, but the amount of freight paid is inflated because of "underweights". (See Finding 85.)

[51] The trade discounts of 5 percent and 3 percent are so prevalent that *Random Lengths* reports its prices as "subject to wholesale discounts of 5 percent and 3 percent on plywood and particle board" (RX's 424A–426Z6; Tr. 402–03) and *Crow's* reports "Plywood and particle board less 5% and 3%." (CX's 879A–U; see also CX 559D; Tr. 354, 402–03, 584–86, 712.) There is, however, evidence of some negotiation of discounts which vary from the industry standard. (CX 90; Tr. 672–73, 714, 719, 1783–84.) A discount of "5 + 5" is given to Georgia-Pacific distribution outlets (Finding 97) and it also appears in inter-manufacturer purchases. (CX 553.) Also widely used in the plywood industry is a 2 percent cash discount for prompt payment. (Tr. 584–86, 811.) The 5 percent and 3 percent discount means, for example, that on a *Crow's* price of $100, first, $5 (5 percent) is deducted; then from the balance of $95, the 3 percent is deducted ($2.85) producing a total discount of $7.85 and a price of $92.15. The 2 percent cash discount is then applied for a net price of $90.31. Note that respondent U.S. Plywood has deducted the 2 percent cash discount *after* first deducting the full amount of West Coast phantom freight from the delivered price. (CX 200.)

[52] Currently, respondents do not regularly issue external price lists (Tr. 1429, 1603; but see Tr. 1741–42 for use by Willamette of a "market letter which contains plywood prices"). Note also that U.S. Plywood substituted *Random Lengths* for its own price list. (CX 860A.)

[53] While prices reported in both *Crow's* and *Random Lengths* are widely used throughout the plywood industry, there can be no question on the basis of a review of all documents in the record, that *Crow's* is the main reference for plywood prices. Although the two publications may not agree on price at all times, the differences are small, and, in fact, may reflect merely different ways of reporting the same information. Thus prior to 1974, *Crow's* often published a "split" or range of prices (hence the industry terminology "low *Crow's*" or "high *Crow's*"). This practice was discontinued in early 1974. (Tr. 354–56.) *Random Lengths*, on the other hand, publishes a straight car price and a higher mixed car price, which in effect shows a discount for heavy volume buyers of straight cars. (Tr. 410; see also Tr. 611; note, however, that when a particular thickness is in short supply (CX 467A), a straight car for that thickness commands a premium over the mixed car price. (CX 466A.)) While the *Crow's* "split" is intended to show a range of prices [50] (Tr. 355), there is evidence that industry members consider the split to be no more than the difference

(Continued)

> [51] Almost without exception, the price of Pine Sheathing to a good credit risk is the low of Crow's or Random Lengths less 5% and 3%. The Crow and Random Lengths split lists [*i.e.*, where a range of prices is reported] generally allude to the low being the straight car and the high applicable to mixed shipments. (CX 811A.)

Similarly, one Boise official, in referring to *Crow's*, said it was "frustrating to realize one man sets an entire industries price yield" (CX 342A), while another yearned for the day "When the plywood industry learns to price their own products instead of letting a reporting service do it. . . ." (CX 346H.) A former Georgia-Pacific branch manager testified that it was no secret that prices were obtained by using *Crow's* (Tr. 956–57, 981), and at Weyerhaeuser "industry price" means the "price appearing in Industry reporters." (CX 882B.)[54]

[52] Despite this proof of the influence of the two publications, the record does not show that the prices reported in *Crow's* or *Random Lengths* fix the base price for all levels of the entire industry. If such were the case — that all mills and distribution outlets were *always*

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between straight and mixed cars, as in the *Random Lengths* reporting. (CX 811A.) As it happens, the *Crow's* "split" often conforms to the *Random Lengths* straight car-mixed car variation. When there is no split in *Crow's*, the *Crow's* price is usually the exact same as the *Random Lengths* straight car price, and in the few instances of differences, the variance is usually $1.00. In sum, the two reporters are in substantial agreement most of the time. Note, for example, in 1970, the following comparison of *Crow's* (C) and *Random Lengths* (RL) prices for 1/2" 3 ply southern sheathing. The *Random Lengths* straight car prices appear in parenthesis.

RL:	65(64)	65(64)	64(64)	65(64)	64(63)
C:	64	64	64	64	63
RL:	65(64)	65(64)	64(63)	63(62)	63(62)
C:	64 to 65	64 to 65	63 to 65	62 to 64	62 to 63
RL:	66(65)	68(67)	68(68)	70(69)	72(70)
C:	64 to 66	67	67 to 68	67 to 68	70
RL:	74(73)	76(75)	75(74)	75(73)	72(71)
C:	72 to 73	75 to 76	75	73	70 to 72
RL:	74(73)	74(74)	76(75)	76(74)	76(74)
C:	72 to 74	74 to 75	74 to 75	74	74
RL:	76(76)	79(79)	83(82)	83(82)	85(84)
C:	76	79	82 to 83	82 to 83	84 to 86
RL:	87(85)	87(85)	86(85)	85(84)	85(84)
C:	86 to 88	86 to 87	86 to 88	84 to 85	84 to 86
RL:	85(84)	84(83)	82(80)	75(74)	73(71)
C:	85	84	80 to 82	75 to 76	72 to 73
RL:	70(69)	70(70)	70(70)		
C:	69 to 70	72	72		

(Source: CX's 674A to 674Z17; RX's 425A to 425Z25.)

[54] The influence of the industry price reporters is such that on Friday, when *Random Lengths'* prices are released, the publisher may receive over 600 telephone calls from subscribers. About 80 subscribers to *Random Lengths* receive the Friday report by Telex. (Tr. 379–80.) *Crow's* has five open telephone lines which are used all day Friday to answer inquiries about the newly published prices. (Tr. 546.) If the Georgia-Pacific's Portland office happens to be closed on Friday, arrangements are made to wire *Crow's* prices to the regional managers as soon as they are published. (CX 546A.)

The testimony of several employees of respondents to the effect that they do not rely on *Crow's* or *Random Lengths* (Tr. 1429, 1672, 2037–39, 2341) is contradicted by other testimony and, more importantly, is contrary to contemporaneous business documents which show overwhelmingly the crucial importance which respondents and the entire plywood industry attach to the prices reported by the two publications. When such a conflict exists, it is the accepted rule in antitrust litigation that contemporaneous business documents not associated with the preparation of litigation are given the most weight. *United States* v. *United States Gypsum Co.*, 333 U.S. 364, 395–96 (1948). I have followed this rule throughout this initial decision.

selling at *Crow's* or *Random Lengths* — then presumably base prices would never change. But base prices in the plywood industry *do* change, mainly as a result of the volatility of the housing industry.[55] Accordingly, all that can be properly attributed to the trade reporters is that each week *starts* with the previous Friday's reported prices (or internal price lists derived from the reporters) as the industry's mill direct prices. (See Findings 93–96.) **[53]**

By the same token, distribution outlets use the weekly mill prices (as reported by *Crow's* or *Random Lengths)* for mill direct sales and as a base for setting their prices for less than carload lots which inevitably are higher than these reported mill prices. (Tr. 785, 916–20 and Findings 97, 98.)[56]

During any given week, however, and particularly when the market is unstable because of volatility in the housing industry, cyclical pressures may operate to move mill prices up or down so that by the end of the week a new mill price may be reported by *Crow's* and *Random Lengths.*[57]

Because of the influence of *Crow's* and *Random Lengths,* the pattern of the industry is that buyers shop in the early part of the week after the preceding Friday publication of *Crow's* and *Random Lengths,* buy on Wednesday, and on Thursday and Friday they await the next edition of *Crow's* and *Random Lengths* to see if the market has been weakened or strengthened. (CX 340A; also see CX's 338C, 572A, 853B for influence of *Crow's* and *Random Lengths* on weekly buying patterns.) **[54]**

93. The use of *Crow's* or *Random Lengths*[58] at respondents' mills as a source of southern plywood base prices (to which West Coast freight is *automatically* added) is shown by the following:

> (a) *Georgia-Pacific.* In quoting southern softwood plywood prices, Georgia-Pacific mill sales representatives use intra-company "Mill Notes" which are derived from *Crow's.* (Tr. 711–12 and Finding 96(a); see also CX 650A.) Departures from

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[55] See Findings 144–151 and CX's 526A–Z70, 546A, 547A, 550A, 554A, 570A, 577A. Not surprisingly, if the market is stable, *Crow's* and *Random Lengths* do not change (CX's 42, 506) and most plywood will be sold at or near the reported prices for more than a week. (CX 860A.) Several witnesses described the movement of plywood prices with anecdotal references to "hourly" changes. (Tr. 785, 1177–78, 1417, 2932.) While such changes "could" conceivably take place, the pattern as revealed in Boise's daily booking prices, is for a fairly stable price to exist during any given week. (See CX's 685A–T and CX's 686A–Z110.) See also CX's 89A–B, where a Willamette official observes that plywood prices "fluctuate *some times* more than on just a weekly basis" [emphasis added] and CX 581 which shows use of a weekly pricing guide at Georgia-Pacific's Crossett Division which requires that variations "must be documented." See also CX 104A which shows use of a weekly mill direct price at Weyerhaeuser.

[56] Transfer prices (which are the basis of the distribution outlet's resale prices and are derived from *Crow's,* see Findings 96–98) are not changed at Georgia-Pacific during an entire week. (Tr. 916–20, 1697–98.) In a rising market, however, Georgia-Pacific branch managers are instructed that prices may be raised in mid-week since many customers prefer to buy at a small increase in mid-week, rather than run the risk of having to pay a substantially higher price during the first part of the next week. (CX 576.) In addition, note that the Weyerhaeuser "CSC's" received a *weekly* national price list which contained a "list" price and a "floor" price. (CX's 104A–B.)

[57] See RX's 69G–Z50 and Findings 144–151.

[58] In all Findings, whenever there is mention of a *Crow's* or *Random Lengths* price, it should be understood that West Coast freight is always added to the *Crow's* and *Random Lengths* price. (See Finding 91.)

Crow's even in the instance of a single thickness to a particular account calls for an explanation at Georgia-Pacific:

> Since this agreement involves pricing in a range below the average of Crow, I will offer an explanation for the variation. Weyerhaeuser is our chief competition on this type of business and they elect to be extremely competitive on 1/2". Occasionally, we elect to meet the situation after conferring with the branch and the regional managers. Besides this account, Lester Lumber Company, we have the situation with E. W. Codwin. There is no problem getting the average of Crow on other thickness. (CX 540.)

(b) *Boise.* During the hearings, Boise witnesses testified that significant changes had been made in the method of doing business at the Moncure, North Carolina mill, and that neither West Coast freight nor *Crow's* are used in the price calculations at this mill. These witnesses claimed that since February [55] 1972,[59] Boise quotes solely on the basis of an F.O.B. mill price, or a net delivered price using actual freight or an approximation thereof from Moncure as depicted in a map (RX 307) showing various zones (zones A to F) radiating from Moncure. (Tr. 2341, 2361–62, 2406, 2460–61, 2483–84, 2486, 2502, 2985, 2988–92.) This testimony must be evaluated in the light of contemporaneous business documents which clearly reveal that Boise has not departed from the industry pattern. Notations made on the Moncure sales manager's desk calendar show conclusively that in 1974 Boise routinely arrived at its Moncure offering prices by starting with the base prices appearing in *Crow's*, deducting the standard industry discounts of 5% and 3% (a factor of .9215), and adding West Coast freight. (CX's 813A–Z30.)

For example, on Friday, August 30, 1974, *Crow's* (CX 928Z13) reported the following prices for Southern pine plywood:

3/8"	1/2"(3 ply)	1/2"(4 ply)	5/8"	3/4"
$91.	$107	$116	$137	$168

Multiplying each price by the factor of .9215 (for the functional discounts of 5% and 3%) and adding the applicable West Coast rate of freight to the most eastern zone where Moncure is located ($2.51 multiplied by association weights, CX's 928Z2, Z3) delivered prices based on *Crow's* plus West Coast freight would be:

3/8	1/2(3)	1/2(4)	5/8	3/4
$112.1065	$136.9005	$145.1940	$172.0455	$210.6620

[56] The desk calendar of the Moncure mill sales manager for the following week (CX 813Z9) shows these entries in the row entitled "Crow's + frt":

3/8	1/2(3)	1/2(4)	5/8	3/4
$112.11	$136.90	$145.19	$172.04	$210.66

Immediately below the "Crow's + frt" notations are the following entries for the so-called "Zone A":

3/8	1/2(3)	1/2(4)	5/8	3/4
$113	$140	$146	$172	$211

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[59] For use of *Crow's* plus West Coast freight prior to February 1972, see Tr. 717–18, 754, 788–90.

If the same calculations are made for all the entries in CX's 813A–Z30 (the desk calendar) and CX's 928A–Z31 (*Crow's*), about 40% of the time the Moncure Zone A prices are exactly the same as *Crow's* plus West Coast freight. In the other nearby zones, there are small additions to *Crow's* plus West Coast freight.[60]

In short, while Moncure's prices are not exactly in line with *Crow's* at all times, whatever differences exist usually result in Moncure prices which are higher than *Crow's* plus West Coast freight. (Tr. 2343–44, 2462, 2992.) There is evidence that Moncure's departures from the usual formula (by charging prices higher than *Crow's*) are well-known in the industry and are attributed to its heavy-selling of mixed loads to the local trade. (Tr. 522–23, 898.)

(c) *Champion*. In "PTS" sales (*i.e.*, when price is set at time of shipment, see Finding 94), the selling prices charged by U.S. Plywood branches to their direct mill [57] customers are based on the *Crow's* prices which appear on the Friday prior to shipment. (CX's 265–66, 269, 271D, H, J, 272A, 273.)

(d) *Willamette*. In addition to the use of the reporters in its substantial volume of "PTS" contracts (See Finding 94(d)), Willamette refers to *Crow's* and *Random Lengths* in setting its spot prices, including its non-contract "PTS" sales. (CX's 29A, 67B.)

(e) *Weyerhaeuser*. Weyerhaeuser ties its direct mill pricing strategy to prices appearing in *Crow's* or *Random Lengths*. (CX's 97, 98, 117, 152B.)

94. Contracts for future delivery of southern plywood invariably have an open-ended price term which is usually expressed as the price appearing in *Crow's* or *Random Lengths* (more often *Crow's)* at the time of shipment, *plus West Coast freight* (calculated on the basis of "association" weights) less the standard industry discounts. These contracts are known in the plywood industry as "PTS" contracts ("Price at Time of Shipment"),[61] in contrast to most spot sales which are made on a "PTO" ("Price at Time of Order") basis. "PTS" transactions are not confined solely to contracts, however; individual orders may be placed subject to a "PTS" term, the price to be determined by referring to *Crow's* or *Random Lengths* on the indicated shipping date. The record shows the following with respect to the use of *Crow's* and *Random Lengths* in "PTS" transactions:

(a) *Georgia-Pacific*. "PTS" contracts for the sale of Georgia-Pacific's southern plywood use *Crow's* or *Random Lengths* as the pricing reference. (CX 650A; Tr. 1469, 1551, 1960–61.) See also CX 133C where a Weyerhaeuser official reported, after a visit with Georgia-Pacific officials, that "most pricing arrangements [in Georgia-Pacific southern plywood contracts] are made based on *Crow's* weekly letter." In [58] 1969, approximately 50% of Georgia-Pacific southern sheathing sales were made to chains or large retail operators pursuant to "PTS" contracts based on *Crow's*. (CX 531.)

(b) *Boise*. "PTS" contracts or orders for the sale of southern pine plywood produced by Boise use *Crow's* as the price reference. (CX's 365Z10 *in camera*, 420F,

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[60] Generally, Moncure's production is sold very close to the mill. (CX 356C; Tr. 722–23, 896, 2459, 2500, 3002, 3020–21.)

[61] "PTS" contracts cover a period of six months to a year. (Tr. 1836, 2289, 2291, 2384.)

Z21, Z36, Z39, Z48, Z51, Z60, Z63, Z66, Z75, Z78, Z81; see also CX 326D *in camera;* Tr. 719–21, 3000.)[62]

(c) *Weyerhaeuser.* It is common practice for Weyerhaeuser to use *Crow's* or *Random Lengths* in "PTS" contracts. (Tr. 1191–92, 2281.) In 1975, 42% of Weyerhaeuser's production was sold on a "PTS" basis. (Tr. 2221–22.)

(d) *Willamette.* Willamette's "PTS" contracts for sale of southern pine plywood are based on *Crow's* or *Random Lengths.* (CX's 29A–B, 67B, 79A–F, 90; Tr. 852, 1783–84, 1835, 1838–39.) Between 1970 and 1974, approximately 40% of Willamette's southern plywood production was sold pursuant to such "PTS" contracts. (CX 29A; Tr. 1835, 1844–47.)[63]

[59] (e) *Champion.* U.S. Plywood's "PTS" contracts (or its proposals for "PTS" contracts) often refer to prices appearing in *Crow's* or *Random Lengths.* (CX's 209A, 215A–B, 216A–B, 219A–C, 227A; Tr. 853–54.)

95. *Crow's* or *Random Lengths* prices are used as the base price (West Coast freight is *automatically* added) in inter-manufacturer sales and purchases of southern plywood. The record shows the following:

(a) *Georgia-Pacific.* Georgia-Pacific's purchase contracts for the future delivery of southern pine plywood are keyed to prices appearing in *Crow's* or *Random Lengths.* (CX's 548, 551, 553, 601A, 609A, 613A–B, 628A–B; Tr. 2132–35.)

(b) *Boise.* Purchase contracts entered into by Boise for its Kingsberry Homes division refer to prices published in *Crow's* or *Random Lengths.* (CX's 336A–C, 353, 361, 366A–B, 397, 404A, 586A, B, F–H; Tr. 2392–93.)

(c) *Weyerhaeuser.* Weyerhaeuser purchases plywood from Willamette at "low *Crow's*" less certain discounts. (CX's 41, 58, 82; see also Tr. 2302.)

(d) *Champion.* The price terms in purchase agreements negotiated by U.S. Plywood often refer to *Crow's* or *Random Lengths.* (CX's 214A, 228A–D, 264, 595A–C; Tr. 2651–52, 2671.)

96. In addition to common use of *Crow's* or *Random Lengths* as base prices in "PTS" contracts or orders, mill sales, and inter-manufacturer sales and purchases of southern plywood (Findings 93–95), the record shows that respondents (with the exception of Willamette which is [60] not vertically integrated) generally transfer[64] southern plywood from their mills to their distribution outlets at

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[62] Approximately 30 percent of Moncure's total 1971 southern pine plywood production was sold pursuant to a "PTS" contract with Wickes in which the price was *Crow's*, less functional discounts, plus West Coast freight. (Tr. 719–21, 786–87.)

[63] Although Willamette sold as much as 55 percent of its total production on the basis of "PTS" contracts tied to *Crow's* or *Random Lengths* (CX 29A; Tr. 1835), this apparently did not deter the vice-president of the company from testifying that he did not rely on *Crow's* or *Random Lengths* as the basis for his prices. (Tr. 1811.)

[64] By use of the term "transfer" I do not mean to imply that these intra-corporate sales are somehow less binding than strict commercial transactions between buyer and seller. At Georgia-Pacific:

> We don't allow the branches to dictate the prices to the mills and we long ago set up that the mills' prices shall be established at the going market prices similar to any outside supplier. (CX 605.)

Note also the following condition imposed by a Georgia-Pacific mill in connection with the proposed sale of plywood to certain distribution centers:

> Failure to perform by either party will be excused only by lack of cars for shipping, fire, strikes, flood, or other major force beyond the control of either party. Market conditions, inventories, price levels, order files, etc., in no way provide either party with a reason for non-performance. (CX 688B.)

(Continued)

prices which are derived from *Crow's* or *Random Lengths*. West Coast freight to the distribution outlets, calculated on the basis of association weights, is added to these reporter-derived base prices. The record shows the following with respect to these intra-corporate transfers: [61]

(a) *Georgia-Pacific*. About 80% of the plywood transferred to the Georgia-Pacific distribution centers from Georgia-Pacific's Building Products Division (the manufacturing arm of the company) is done on an "allocated basis."[65] (Tr. 1573–74.) The transfer prices for allocated sales are communicated to the centers through so-called "Mill Notes". (Tr. 1387–88, 1574.) The Mill Note base prices are taken from *Crow's*. (CX's 526A–Z64, 528, 592A, 602B–603, 607B, 617A, 637–641, 645A, 646A, 647A, 648A; Tr. 934–35, 937.)[66] Note in CX 617A a Mill Note was revised because the published *Crow's* price was different from an earlier, orally communicated transfer price.

The delivered prices in transfers of southern plywood to the Georgia-Pacific distribution centers, whether "allocated" or not, include West Coast freight. (CX's 537, 544A, 600A, 614A, 637, 645A, 646A, 647A, 648A; Tr. 921–22, 934, 1390–91, 1545–47, 1948.)[67]

[62] (b) *Boise*. Boise's Moncure mill contracted with the Boise "BM & S" Division for the transfer of a fixed amount of southern plywood to certain "BM & S's". The transfer price for this contract, which was entered into in 1971, was determined by deducting functional discounts from the price reported in *Crow's* two Fridays prior to shipment. (CX 387; Tr. 2477–78; see also CX 322B *in camera*.)

In this Moncure-"BM & S" contract there was a variation from the usual industry formula of using West Coast rate less actual freight. Under this contract, the Boise "BM & S's" paid a freight charge of $1.80 per hundred-weight (derived from the West Coast rate of $2.07, less 27¢ per hundred-weight, the average freight cost to the destinations normally shipped by Moncure), plus actual freight from the mill to each "BM & S". (CX's 387A–B; Tr. 2477–78.) While this departure from the standard industry formula resulted in some differences in the prices to each "BM & S" within the same West Coast freight zone, nevertheless, in this instance, too, a transfer price was used which included freight derived from the West Coast rate rather than the sharply lower actual freight rate. (CX's 387A–C, 390.)

(c) *Weyerhaeuser*. Since 1971, plywood produced at Weyerhaeuser mills has been transferred to the Weyerhaeuser "CSC's" at the average of prices reported in *Crow's* and *Random Lengths* plus West Coast freight. (CX 131; Tr. 1142, 2227–29, 2267–68.)

(d) *Champion*. Plywood produced by U.S. Plywood's mills is transferred to the

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See also CX 647A ("These are firm and non-cancellable orders on the part of either party except for force majeure") and Tr. 1554 where the Georgia-Pacific official in charge of mill sales testified "We stand at arm's length with the Distribution Division [branches], so to speak."

Specifically, I do not find credible the testimony of Georgia-Pacific officials that transfers are simply an internal method of dividing up the "pie". (Tr. 1578, *et seq.*) Contemporaneous documents and other testimony prove that transfer prices have a far more pervasive influence on the plywood market. (See Findings 97, 98.)

[65] Under the allocation system, each Distribution Division region agrees with the Building Products Division that a fixed amount of softwood plywood will be transferred each week to each region. The regional manager then sets an allocation to be shipped weekly to each branch within his region. (CX's 559M, N, 645A–648B; Tr. 960, 1573–74.)

[66] The record proof showing reliance on *Crow's* is not diminished, and, in fact, is supported by the equivocation of the Georgia-Pacific vice-president in charge of the distribution centers who testified that the company uses "some sort of market report service transfer cost." (Tr. 1574.)

[67] Note that in all transfers where the base price is *"Crow's"* (*i.e.*, CX's 526A–Z64) West Coast freight is added automatically. (See Finding 91.)

> branches at transfer prices established on **[63]** Friday of each week. These prices are intended to reflect the current mill prices. (CX 177B; Tr. 2581–85.) Usually these prices are identical to the *Crow's* prices. (Tr. 1021–22, 2689.) Moreover, the transfer price charged a U.S. Plywood branch for a direct mill shipment to the branch's customer is tied to the *Crow's* price Friday prior to shipment. (CX's 252, 253A, 256–260, 271D, 272A.)
>
> On all transfer sales, U.S. Plywood charges its branches transfer prices which include West Coast rail freight. (CX's 203A, 232A, 233B, 234A, 235A, 236A, 237A, 239A, 240A, 241A, 242B, 243A, 244A, 245A, 246B, 247A, 248B, 249A, 250A, 251A, 263, 274–78; Tr. 1000, 1006–07, 2613–14, 2713.)

97. As for use of the trade reporters at the distributional outlet level once the plywood is transferred, the record evidence indicates that the distribution outlets set their basic offering prices by relating them directly to transfer prices, which, in turn, are drived from *Crow's* or *Random Lengths*. As indicated earlier, all of these outlets are profit centers. (Findings 38, 42, 47, 51.) This means, for example, that Georgia-Pacific distribution centers, which buy straight carload quantities from the Georgia-Pacific mills at *Crow's* less a discount of 5 percent and 5 percent plus West Coast freight (CX 325B; Tr. 925–26, 934),[68] must then set their carload prices for mill **[64]** direct shipments (*i.e.*, when the branch makes the sale, but the wood is shipped directly from the mill) at *Crow's* less a discount of 5 percent and 3 percent plus West Coast freight. (Tr. 927, 931, 934.)[69] For inventory sales or for sales of smaller or mixed quantities, additions are made to this basic price at the Georgia-Pacific branches. (CX's 566A, 580B, 610A–i; Tr. 783, 919–20, 928, 931, 934, 977–78, 4386–87; see also Finding 98.)

Similarly, the Weyerhaeuser "CSC's" are told to "price at mill direct levels [*i.e.*, carload price] plus a distribution margin." (CX 896; Tr. 1150–51, 1168–71, 1173–75, 2262–63, 2266–67.)[70] The U.S. Plywood branches buy on a carload basis which includes West Coast freight (CX 811A; Tr. 1006–11, 2613–14); to this transfer price the branches add a markup based on the number of pieces ordered by their customers. (Tr. 1016.)

98. As shown in Finding 97, branches use the transfer prices of carload lots, that is, the current replacement cost of a carload, as reported in *Crow's* or *Random Lengths*, as the basis for their mill direct

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[68] The two "5's" discount was also used at U.S. Plywood. (CX's 182A, 325B, 352A; Tr. 811.) Larger discounts are given on certain items for the very purpose of encouraging the distribution outlets to be more aggressively competitive in securing a greater share of a particular market. These "deals," see, *e.g.*, CX 533, 580C, show the direct connection between transfer prices and resale prices. See also CX's 104A–B, 106A–B, 111A, 114A, 182A–D, 212, 509, 510, 517A–B, 527, 531, 535, 537, 541, 559H–i, 574, 811A and Tr. 1426 for additional proof of the relationship between transfer prices and branch resale prices.

[69] See also CX's 603–04 which refer to a "Customary Initial Percentage Markup" of the Georgia-Pacific distribution centers. This markup is added to *Crow's*, the mill direct price.

[70] Prior to 1971, plywood was transferred to the "CSC's" at the Weyerhaeuser mill direct carload price. (Tr. 2266; but see CX 109C for use of *Random Lengths.)* After 1971, the average of *Crow's* and *Random Lengths*, *i.e.*, the industry's direct mill price, was used. (See Finding 96(c)).

prices as well as their out-of-inventory less-than-carload prices. Clearly the managers of these distribution outlets must ordinarily sell less-than-carload lots at **[65]** prices above the mill replacement cost of a carload.[71] As a former Georgia-Pacific branch manager put it, "Down at the branch level, we knew our cost, and we couldn't play with it too much because the percentage of profit was too low." (Tr. 954.)[72] In fact, the only reason for having branches is that they provide a package of services to local customers which enable them to sell out of inventory in smaller (break bulk)[73] quantities *above* **[66]** the *Crow's* or mill direct carload prices. (See Finding 97 and Tr. 1151, 2194, 2199, 2256–57.) Note in this connection, that a spokesman for the Georgia-Pacific distribution outlets wrote that unless the outlets are able to buy from the Georgia-Pacific mills at "low *Crow's*" rather than "mid *Crow's*" (when *Crow's* reported a split price) they could not warehouse and redistribute to chains and other large operators which buy on the basis of the average of *Crow's*. (CX 531.)

A record of losses — in other words, sales *below* replacement costs (*i.e.*, the mill direct or "*Crow's*" price) — affects the profitability of the branch as well as the compensation and job security of the distribution outlet manager.[74] **[67]**

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[71] Georgia-Pacific personnel are specifically instructed not to set their plywood prices on the basis of average cost, but rather on replacement cost. (CX 576; see also CX 644A.) At U.S. Plywood, where sales out of the branch are "all based on the transfer cost" (Tr. 1032), actual average cost is not used; instead, branch prices are based on current mill prices. (Tr. 1033.) Specific transactions at respondents' branches may be negotiated at prices below the *average* transfer prices. (Tr. 973–74, 1034, 1577, 1581.)

[72] Plywood is sold by a branch in a quantity known as a "bunk" or "unit" which, typically, consists of a stack of plywood 30 inches to 33 inches high, the surface measure volume of which depends on the thickness of the plywood (*e.g.*, a "unit" of 3/8 inch plywood contains 2,816 square feet, surface measure). A truckload varies between 12 to 16 units. A full carload consists of approximately 36 units. (CX 581; Tr. 1956, 1968.) Distribution outlets rarely sell full carloads from inventory (Tr. 1017, 1719) but they do arrange for direct mill shipments of such quantities. (CX 549; see also CX 814; Tr. 971, 2572.)

[73] There is evidence, however, that in a severely depressed market, such as the recession of 1974–75, the usual pattern of the industry may not always prevail, and wholesale prices below mill direct prices do occur. (RX's 69G.) See also RX 312 and CX 661 where sales out of warehouse at prices lower than *Crow's* in 1970 and 1973 are newsworthy items.

[74] Tr. 814, 937–39, 954, 1711, 1945, 1969–70, 2000, 2027–28, 4386–87. Several officials of respondents testified in sweeping generalities that transfer costs have "no" effect on distribution outlet prices. For example, one high official of Georgia-Pacific said the transfer price has "nothing to do with what they can get for the plywood, but if we are transferring at a higher price than they can resell it for, why they are going to yell." (Tr. 1560.) They "yell" because "They have to make a profit." (Tr. 1561.) A similar pattern prevails throughout the record — first, an unequivocal (and unbelievable) statement that transfer costs have nothing or little to do with resale prices, followed later by a retraction saying that transfer prices happen to impact very directly in several crucial areas, namely, the profitability of the distribution center as well as the compensation and employment security of branch managers. Compare, for example, Tr. 2008 (no relationship between transfer cost and prices) with Tr. 1998–99, 2000, 2027–29 (the object of a distribution center is to show a profit) and Tr. 2265 (distribution outlets should worry if they do not cover costs). See also Tr. 4213–14 which shows that transfer prices are used to determine the profitability of the producing mill.

While the record shows that branch managers have discretion in setting their prices and that these prices respond to market conditions (Tr. 771, 810, 928, 931, 934, 1014, 1172, 1586, 1596, 1601–02, 1891–93, 2224), the economic realities of the plywood industry, as indicated in the text of this Finding, dictate that this discretion be limited by the requirement that branch prices be above the direct mill level. As the record plainly shows, the distribution outlets are economically justified only if they are able to provide services which produce a higher than direct mill price. Moreover, as profit centers, they have every incentive to sell above the direct mill price since the inevitable result of prices lower than their costs is that they would be phased out as unprofitable.

99. In sum, at all levels of distribution southern pine plywood is sold on the basis of a formula — well known to the entire industry — that the basic prices are *Crow's* or *Random Lengths* prices or within a narrow range of *Crow's* or *Random Lengths* prices, that certain standard discounts are usually taken from those prices, and that West Coast rail freight multiplied by "association" weights is added to these base prices. (Findings 72–98.)[75] Thus shortly [68] after the Georgia-Pacific's Russelville, South Carolina mill opened, a local competitor could confidently report:

> They [Georgia-Pacific] have adopted the following price basis. Low Crow's less 5% less 3% plus West Coast freight. (CX 880.)

And *Crow's* is obviously reflecting industry custom when it says routinely week after week that a 5 percent and 3 percent functional discount is taken off its reported prices and

> Addition of Portland freight to Southern Pine prices will provide approximate delivered costs. (CX's 928C–Z31.)

100. The weight of the evidence is that in sales from respondents' southern mills to southern branches, at any given point in time, respondents use a single base price for southern pine, but not necessarily the same price.[76] With the addition of West Coast freight, this results in the same delivered price to each respondent's southern distribution centers within the same West Coast zone. Similarly each respondent's direct mill customers, who are located within the same West Coast zone in the South, are charged the same delivered prices though these direct mill customers (including customers with multiple outlets) may be located at unequal distances from the mills. (CX's 2A,

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[75] The exact calculations are easily made. Using the price appearing in *Random Lengths* dated November 14, 1975 (CX 680A) as a "mill price," the delivered price of a shipment of 1,000 square feet of 1/2 inch CD - Exterior Glue 3-ply southern pine plywood to a customer in the most easterly West Coast freight zone is as follows:

Reported price	$115.00	
Less discounts of 5% and 3% ($115 x .9215)		105.97
Freight Calculation		
Freight rate: $2.79 per 100 lbs.		
Association Weight of 1/2 inch equals 1525 lbs.		
Freight Cost equals 1525 divided by 100 x 2.79 equals		42.55*
Total delivered price		$148.52

(CX's 680A–B; Tr. 408, 1933–34)

*Note: Freight computation is made by *Random Lengths, e.g.,* freight for 1/2 inch, 1525# in 2.79 zone is $42.55. (CX 680B.)

[76] It should be emphasized that the evidence discussed in this Finding relates solely to the question of price uniformity in sales to distribution centers and customers of each respondent. Complaint counsel failed to prove that respondent's practices result in exactly matching prices to all customers or to all branches (see Finding 143) even though *Crow's* and *Random Lengths* are widely used as the industry's base price.

10, 11, 112B, 212, 884H, 886Z29; Tr. 713–14, 720–21, 847–48, 857–58, 1017, 1142, 1157–58, 1163–64, 1189, 1200, 1546, 1559, 1839, 2131, 2253–54, 2713–16, 2719.) See, however, Finding 142 for evidence that respondents attempt to impose add-ons or "upcharges" to more distant northern customers **[69]** within the same West Coast freight zones who are located outside of the primary southern marketing area. In addition, see Finding 96(b) for evidence that Boise, in dealing with its southern distribution centers, adopted a slightly different formula which added actual freight to a phantom freight figure to arrive at different delivered prices to each Boise "BM & S."

While distribution outlets of a particular respondent usually use a single delivered price in their assigned territories (Tr. 813, 1016, 2041), local market conditions may result in variations in the delivered prices to particular localities within the same West Coast freight zone. (Tr. 735–36, 811, 1181, 1196–97, 2238–39.)

101. Respondents' officials and ex-employees testified generally that they are not able to predict the future plywood prices of their competitors in a given market. (See Tr. 1489, 1681, 1813, 1944, 2238, 2483, 3004.) This testimony must be evaluated in the light of what respondents actually did; namely, they removed a large element of uncertainty which would have existed in the southern plywood industry but for the adoption of a uniform and predictable West Coast freight rate that is predictably added to base prices derived from the industry reporters. On the subject of predictability, it must be emphasized that when a Champion sales manager writes that "almost without exception the price of Pine Sheathing to a good credit risk is the low of *Crow's* or *Random Lengths* less 5% and 3%" (CX 811A), it is understood in the industry and it is completely predictable that West Coast freight will be added to the *Crow's* or *Random Lengths* prices, as plainly indicated in the publications themselves. (See Findings 88, 91, 99.)

On the other hand, the record shows that uncertainty still exists in the plywood industry because of the volatility of the housing market and, as indicated earlier, the *Crow's* and *Random Lengths* prices respond to cyclical pressures. (Finding 92.) But all cyclical pressures are duly reported by *Crow's* and *Random Lengths* (RX's 69E–85), and whatever the new price level may be, the new week in the southern plywood industry invariably begins with *Crow's* or *Random Lengths* plus West Coast freight. (Findings 92–98.) **[70]**

West Coast Freight as a Focal Point of Southern Plywood Pricing

102. Not only did use of the West Coast rate and "association"

weights eliminate a large measure of uncertainty which would have resulted from the use of the southern freight rates but the West Coast freight factor also served as a focal point for an industry-wide plan to resist passing on locational advantages to purchasers, and to add phantom freight to gross margins, as originally contemplated by Georgia-Pacific. (Findings 103–112.)

103. The significance of West Coast freight as a focal point for resistance to price cutting is shown in contemporaneous documents. Freight "pick-up" or freight "gain" — the industry's euphemisms for phantom freight — is considered to be so pivotal to pricing in the southern pine industry that respondent Champion admonishes its field personnel,

> We have had reports on pine prices that caused the conjecture that someone was playing with the freight pick-up, but we have had no evidence that this is true and the base price has been the culprit. This is a very delicate area and all loose talk on this subject by our branch managers and salesmen should be curtailed. We should not, in any way, endanger this necessary source of income by getting involved in any tale carrying or rumor spreading, as this would be a fatal blow to the southern pine industry, which is in no great shape with the freight pick up, let alone without it. (CX's 181A-B.)[77]

[71] 104. In 1966, a Georgia-Pacific official observed "Freight appreciation has been remarkably stable during the entire year." (CX 502B.) Five years later, the policy of preserving freight "pick-up" or "gain" is still so central to its southern pine plywood business that Georgia-Pacific personnel are advised,

> Since we have made a strong commitment to protect freight gain, I feel that we should guard it closely and make any necessary market adjustments in the mill price. (CX 564.)

105. At Weyerhaeuser,

> . . .the key to the SYP [Southern Yellow Pine] Plywood business is freight return, the dollar difference between the West Coast freight rate and the actual freight rate. Our target is 1.25/CWT. This target is an arbitrary figure but past experience indicates it is a fairly realistic figure. (CX 137A.)

106. That phantom freight is a focal point of southern plywood pricing is further shown by respondents' practice of constructing elaborate tables showing the amount of freight "pick-up" (phantom freight) which is available depending upon the location of the

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[77] The attempt of Mr. Kelley, Vice President of Champion, to explain away this document on the witness stand in terms of a special situation relating to uneconomical shipments to the Chicago area or upper Midwest is not credible. His recollection on the witness stand was hazy at best (compare Tr. 2648–50 with Tr. 2749–51), and nothing he said changes the plain meaning of the document itself which shows a *general* concern for preservation of phantom freight. (See Tr. 27, 33–35.)

customer. Respondents' marketing strategy is then directed toward either preserving this freight "pick-up" or minimizing freight "loss."[78] (CX's 17A-J, 26A-Z25, 40A-B, 41, 88A-L, 91A-Z74, 92A-Z72, 137A-B, 142A, 181A-B, 182A-D, 183A-B, 188, 324A-J, 350F *in camera*, 356C-D, 364i-J *in camera* 422A-E *in camera*, 488A, F, 490A-B, 491A, F, 492A, C, 493A, C, E, 495A, D, 501A, D, 522A, H, 556A, 559A-Z45, 563A-B, 564, 565A-B, 566A-B, 573A-B, 574, 580A-P, 883A-C; see also a 1965 survey by a non-respondent producer which comments on "how all-important this comparative rate structure is [the difference between actual and West Coast freight].") (CX's 665D-E.) [72]

107. So well-accepted is the notion of freight "pick-up" in the southern plywood industry that one respondent informs another about its progress in preserving this locational advantage. The vice-president of Willamette apparently told a Boise Cascade official of the amount of 1968 freight "pick-up" which accrued to Willamette as a result of the difference between West Coast and actual freight. (CX 333D.)

108. Because of the importance assigned to phantom freight by respondents, a freight rate *increase* is considered an "advantage." Just such an increase inspired the following reaction by a Willamette official:

> *Advantages – Plywood*
>
> Using as an example 1/2 inch plywood on 1525 lbs. per thousand square feet the Ruston, Louisiana to Washington, D.C. rate has increased from $.75 to $.79 and the coast rate from $1.75 to $1.84 per cwt changing the southwestern rate advantage from $15.25 per thousand square feet to $16.00 per thousand square feet (up $.75 per thousand square feet). This, of course, gives us an advantage in Louisiana in that we market our products from that location at the coast rate thusly taking advantage of an additional freight pickup or at least allowing us to reach further marketing areas at the same freight rate pickup. (CX 862A.)

109. The concept of freight pick-up is included in plywood contracts. For example, there is the following language in a Willamette — Weyerhaeuser agreement:

> Sales are restricted to our normal sales area of the Southeast and surrounding states as outlined on the attached map. We will accept an occasional car in the close perimeter, outside this area such as Chicago, Cleveland, or Detroit; but, in turn, Weyerhaeuser will give us a car close to our mills so we can maintain our freight pickup. [73]
>
> The final approval of such a destination is for us to say. (CX 41.)[79]

110. In the southern pine plywood industry, the use of West Coast

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[78] Also sometimes called freight "return," freight "premium," freight "advantage," freight "allowance," and freight "gain."

[79] See also Tr. 1784 and CX 628A for additional proof that southern pine contracts are negotiated in order to realize an average or minimum amount of freight advantage.

freight rate and the association weights are not subject to negotiation: bargaining, therefore, is confined to dickering over the "base" or *"Crow's"* price. This is shown by the fact that a substantial volume of southern plywood is sold on a "PTS" contract basis where the only price term negotiated is whether or not a small discount or premium is to be taken from or added to the mill base price appearing in *Crow's* (or *Random Lengths*) at the time the order is shipped. (Tr. 582, 698–99, 719–20, 1191–92, 1469, 1558, 1783–84, 2219, 2384–85.)[80] West Coast freight, multiplied by association weights is automatically added to these base *Crow's* or *Random Lengths* prices. (See Finding 76.)

It is particularly noteworthy that "PTS" contracts are negotiated with respondents' "best customers" and unless the prices to these buyers are "reasonable" or "equitable," this large volume business could not be retained. (Tr. 2220, 2280–81; see also CX's 78A–B.) It is unlikely that knowledgeable and important "PTS" buyers (say, a large chain like Lowe's, see Tr. 2719–20) would agree to buy at *"Crow's"* (a typical "PTS" price term) if there is a pattern in the industry, at any given time, of a large volume of production being sold under *Crow's* plus West Coast freight.[81]

[74] 111. In spot sales, too, competition in the basic plywood price — the mill price for a carload (whether sales are made by the mill itself or by the branch and then shipped mill direct) — is kept within a narrow range. As U.S. Plywood's Southeast Regional Sales manager put it, "Almost without exception, the price of Pine Sheathing to a good credit risk is the low of *Crow's* or *Random Lengths* less 5 and 3%." (CX 811A.)[82] See also, Tr. 981 ("Everybody knew the formula [*i.e.*, *Crow's* plus West Coast freight]. So if you were out of line you didn't get the order") and Tr. 977 ("normally your customer [for a full carload] knew the cost of that plywood before he ever even called you up, because he

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[80] The size of the discount depends on volume and specifications. (CX 326D *in camera*.) Another factor in "PTS" negotiations is the mix of the contract. (Tr. 2278–79.) For indication of how slight the variations are in "PTS" contracts, see CX's 79A–F.

[81] Note, however, that a plywood producer may decide not to enter into a "PTS" contract for the reason that he anticipates selling *above Crow's*. (See Tr. 3000.)

[82] See, however, CX 210A, B where in response to CX 811A a U.S. Plywood official observed "There are a good many reasons for. . .spreads in a given items prices such as the mix in the order, the freight pickup involved in the South and the underweights involved in the West and whether shipment is via truck or rail and the discounts." When this official, however, described prices as "all over the map depending on who wants to buy what and how much and who wants to sell what and how much" he relates this to a dollar or two off current list prices. Note also that the *Random Lengths'* plywood prices are published subject to the following caveat explaining price variations:

> For sheathing slightly higher prices are applicable to assortments of several items or when combined with sanded. (CX 680A.)

In addition, see Tr. 348 for indication of quantity discounts to particularly large buyers and CX 326C *in camera* for higher prices to customers "who need quick shipment and will pay a premium for a particular car." Still another explanation for price differences is that in the period of price controls, between August 1971 and mid-1973 (Tr. 1725–26), when demand was particularly heavy, different ceiling prices prevailed among producers. But for this unusual situation, a Georgia-Pacific official recognized that "these variations would melt away." (CX 602A.)

also had access to the same costing information that everybody else had"). [75]

Should one mill's price be substantially different from the others, this is usually a sign that the variant mill does not want to sell its plywood. (Tr. 2126–29.) See also Tr. 422 ("Maybe they [Boise-Cascade] want to just pull off the market so they just stick a price up there and say, 'Well, this ought to keep the customers away for a while, while I consolidate my shipping file' "), and Tr. 2783 where an unusual mill price ("considerably below the market") is characterized as a sign of a temporary loss leader which quickly evaporates.[83] In contrast to these anecdotal differences, there are genuine cyclical pressures, essentially related to the housing industry, which require mills to sell above or below the previous week's *Crow's* or *Random Lengths* with the result that price differences develop. From these price differences, the price reporters make a judgment call as to where most mills are priced and this becomes the reporters' prices for the next week. (Tr. 421.)

112. At the distribution outlet level, branches attempt to price above the direct mill carload level ("whatever the traffic would bear," Tr. 934 and Findings 97–98) for a truckload, a bundle, or a single sheet of plywood. The quantity purchased, the urgency of the delivery, and the attractiveness of the "mix"[84] of the order (whether [76] other profitable lumber products are being purchased besides plywood) result in price variations. (CX's 104A–B; Tr. 783, 919–20, 1016, 1591, 1893, 1902, 1955–58, 2036, 2766, 2784, 2960.) The extent and intensity of these price variations — that is, different prices *above* the direct mill prices with differences reflecting quantity, delivery, and mix — depend on local market and competitive conditions. (CX's 104A–B; Tr. 928, 931, 934, 2036, 2849.) In a market with some weakness, the range in an inquiry involving a mixed purchase of 1/2 inch CDX and 5/8 inch CDX was from $149 to $153 for the 1/2 inch. (Tr. 2776.) When the market is stable or strong, the price quotes are within 50¢ of each other. (Tr. 2779.) On the downside or in a rapidly rising market "exceptionally " large spreads in prices appear such as $7 to $8. (Tr. 2780–82.) See also Tr. 2892, where a dealer called by respondents testified that 30 to 40 percent of the time, price quotes differ by less than one dollar, and the usual range was between $1 to $3. The record shows, moreover, that price variations quickly evaporate. Thus a sudden increase or decrease in distribution outlet sales is a signal to a

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[83] While the industry reporters have on occasion reported sharp price differences (see, *e.g.*, RX's 69o, P–Q, Z42, Z43), it is significant that *every* week the reporters are able to announce *one* price for each item. The publisher of *Random Lengths* testified:

> We can get a range of prices from the individual sources that we contact, I suppose an average would be a range of $5 to $7. But then, as you narrow, or, as you look at this range, you take all of the prices, their [sic] emerges a more common price at which most people are priced. (Tr. 421.)

[84] For the significance of "mix" in plywood sales, see Tr. 2257–58.

branch manager that his price is too low or too high and an adjustment is made. (Tr. 1892.)

Effect of West Coast Freight on Locational Decisions

113. Operators of southern plywood mills prefer to ship east of the mill where the West Coast freight rate increases, rather than to the west, where it decreases. This preference appears, for example, in this early policy statement of Willamette officials respecting their Ruston, Louisiana, mill:

> Frankly, Bill, we can move it to much better advantage pricewise, east of us, rather than going into Texas, Oklahoma, Kansas or Missouri. In fact, we are at a great disadvantage in going into Oklahoma or Kansas particularly.
>
> At the present time in Texas we have been offering our stock only into the Fort Worth - Dallas area. We do not have any one in the [77] Houston area, but have quoted a few cars for this area. The only other areas you have yards in that we have been quoting to is around St. Louis, and, again, around Kansas City there is a disadvantage to us.
>
> As you have outlined in your letter, if we are going to sell in the Texas area, we are going to have to sell it on the basis of competing with the $1.19 coast rate. Then if we add the cost of trucking, it makes it a disadvantage over what we can get into such areas as Georgia, Florida, or other Southern States. For instance, we have a trucking rate into Fort Worth of .40¢. If we deduct this from the $1.19 coast rate, this gives us only a .79¢ advantage where if we can sell this same material into Georgia or Florida on a $1.54 rate with only about a .50¢ or .60¢ rail and truck rate, it gives us a net .90¢ to $1.00 advantage, which dollar and centwise is better than we can do into the Texas area.
>
> Of course, if we had a tremendous production we could not pick and choose like we are doing at the present time, but unless this company puts up another mill some place I do not think we will have over 5 million feet a month, and that could be a year away. At the present time, we are only looking for 3 or 4 million feet a month total production. (CX 9A.)[85]

114. Since the freight "pick-up" is a function of West Coast freight less actual freight, respondents not only prefer to sell east of the southern mill (thereby increasing West Coast freight), but they also prefer to distribute close to the plant, thereby decreasing actual [78] freight. (CX's 99X–Z, 573A, 665D; Tr. 514–15, 1198–99, 2612, 2737.)

115. Complaint counsel failed to prove that the two locational influences described in Findings 113, 114 — the preference for shipment east and the desire to reduce actual freight — have operated to create disincentives to the most efficient geographic location of producing points or disincentives for customers to locate close to producing mills, as alleged in the complaint. (Complaint ¶'s 18(c), (d).) In the absence of any direct evidence on how sites are chosen, I believe

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[85] See also CX's 1A, 2A, 10, 11, 17A–J, 26B–C, 91A–92Z72, 861.

it is fair to conclude that both sellers and buyers may choose to locate in a particular location for reasons of availability of raw material or proximity to consuming markets which have nothing to do with the denial, or for that matter the receipt, of a geographic advantage due to use of the West Coast freight rate.

116. While the systematic use of West Coast freight less actual freight, means that respondents' mill net returns may differ depending on consumer location, complaint counsel failed to prove that this results in economically meaningful "discrimination in prices between customers" as alleged in Complaint ¶ 18(b). To the contrary, the weight of the evidence is that *all* southern pine plywood customers of respondents are disfavored since they all pay phantom freight based on a distant West Coast base.

Cost of Phantom Freight

117. The West Coast freight rate used in the sales of southern pine plywood is recognized by respondent Champion as phantom freight. (CX 200.)

118. Because plywood is a relatively heavy product, shipping costs are an extremely important part of the total delivered price. Depending on the buyer's proximity to the mill of origin and the base price, the freight [79] cost may amount to as much as 30 percent of the total delivered price.[86]

119. Actual freight from respondents' southern mills is substantially less than the West Coast phantom freight which is included in southern plywood delivered prices. To illustrate, in 1972 actual freight from Georgia-Pacific's Chiefland, Florida mill to markets in Tampa, Orlando, Tallahassee, and West Palm Beach, Florida, ranged between 14¢ and 21¢. The West Coast rate to these cities was $2.01, resulting in an average freight pick-up of $20.8575 per thousand square feet. (CX 580E.)[87] For references to detailed tables showing the enormous freight "pick-up" which accrued to respondents from use of West Coast freight, see Finding 106.

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[86] See, *e.g.*, CX's 928Z28, Z29, which show a *Crow's* price for 1/2 inch 3 ply (southern) of $87.00, and a West Coast rate to the most easterly zone of $38.30 for a weight of 1525 lbs., the "association" weight for 1/2 inch 3 ply. In this example, the freight is 33 percent of the total delivered price of $125.30. For actual invoices showing similar freight charges, see CX's 867–72, 875–76.

[87] See CX's 205A–B which shows a customer in Savannah, Georgia, buying from a U.S. Plywood warehouse in Savannah, Georgia, and paying freight costs ranging from $12.15 to $34.25 per 1,000 square feet for this intra-city shipment, depending on weight of plywood purchased. See also RX 87 which shows current actual freight from Georgia-Pacific's Savannah, Georgia mill to Miami, Florida of 57¢. The current West Coast rate to this zone is $2.79. (Tr. 1392.) On a shipment of 1,000 square feet of 1/2 inch plywood (1525 lbs. according to "association" weights), the difference between actual and West Coast freight would result in a freight "pick-up" of $33.86 per 1,000 square feet.

Effect on Choice of Means of Transportation

120. Southern pine plywood cannot be picked up by a customer's truck at a true F.O.B. mill price in order to save the cost of West Coast freight. (CX's 113B, 880.) **[80]**

121. Instead of allowing mill pick-ups in the customer's own truck at a true F.O.B. price, the practice followed by all respondents, should the customer (including distribution outlets in intra-company transfers) elect to pick-up in his own truck, is to take the delivered price, *which includes West Coast rail freight*, and allow a small discount (usually $2 to $4 per thousand feet) or in the case of Willamette the actual truck freight cost, as a pick-up "allowance." (CX's 5A, 9B, 15A, 487B, 511, 515, 520A–B, 557A–558B, 562, 580C, 583B, 596A–C, 885Z1, 886Z26; Tr. 717–18, 741–44, 1009, 1030, 1184–85, 1632, 1691, 2592–93.)

122. Truck pick-ups by customers of respondents are at a minimal level. At Georgia-Pacific, it is 1 percent of plant production. (CX 487B.)[88] There are relatively few truck pick-ups at Weyerhaeuser "CSC's" (Tr. 1183, 1185) or Champion mills. (Tr. 2701.) Mill pick-ups at Boise's Moncure mill were 4.6 percent of 1971 shipments and 1.3 percent of 1972 shipments. (CX's 441L. 442S.) The Moncure mill had no pick-ups in 1973 (CX 401; Tr. 2502–03), but in 1974 customer truck pick-ups increased. (RX 347A; see also Tr. 2376.)

Exchange of Information

123. There is no charge in the complaint and no proof was presented by complaint counsel that respondents met and formally conspired to add West Coast freight, or to adopt "association" weights, or to use *Crow's* and *Random Lengths* as a handy base price reference. But there can be no doubt that as customers of each other, and as members of the same trade association (American Plywood Association),[89] there are ample opportunities [81] for each respondent to familiarize itself with all the basic policies of the other respondents, including the use of West Coast freight. (See Findings 79 and 95 and CX's 34, 325B, 327, 333D, 352A; Tr. 2703–04.) Moreover, the record contains direct evidence of the exchange of information among respondents which relates to the southern plywood pricing formula discussed in earlier Findings. For example, a Weyerhaeuser representative could infer from a discussion with Georgia-Pacific's mill sales manager that Georgia-Pacific did most of its "PTS" contract pricing based on *Crow's*. (CX 133C; see also CX 142.) Willamette's senior vice-

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[88] In March 1971, Georgia-Pacific did not allow customer truck pick-ups at their mills. (CX 559E.)

[89] At a meeting of the American Plywood Association, Weyerhaeuser and Georgia-Pacific representatives had "conversations which ranged from customer commitments to plywood marketing practices." (CX 133A.)

president apparently furnished Boise Cascade with the amount of freight "pick-up" realized by Willamette in 1968. (CX 333D.) And a Georgia-Pacific official reported:

> Incidentally, Jimmy Schmidt, Sales Manager for Boise's Southern Pine Mill in North Carolina, was in the office last week and indicated that they are making all their 1/2 inch in 3-Ply construction and are selling it all at not to exceed $1.00 under the 4-Ply/5-Ply. (CX 593.)

"Justification" for Use of West Coast Freight

124. According to respondents the only significance of West Coast freight is that it is "backed off" the delivered price to achieve a so-called "index" price which allows ready comparisons between the price of Douglas fir plywood and the price of southern pine plywood. (Tr. 1626–27, 1744–45, 2032, 2201–03, 2276.) While it is true that the use of West Coast freight does allow ready comparisons between southern prices and western prices, as well as between prices of competing southern producers (see Finding 82 and CX 51), the record shows overwhelmingly that West Coast freight is *added* to a base price (not "backed off") for the purpose of arriving at a delivered price which approximates the delivered price of Douglas fir. (Findings 65–79, 89–99, 102–08, 129–30.) [82]

125. Respondents also argue that the use of West Coast freight is justified because their customers *wanted* southern prices which could easily be compared to western prices, particularly at the outset of the southern pine plywood industry. As indicated in Finding 124, the record supports the contention that the industry-wide method of pricing — *Crow's, Random Lengths* or base prices derived from these reporters, plus West Coast freight — results in plywood prices, both western and southern prices, which are easily compared, and that respondents' customers may even favor this method of setting prices. (CX's 51A–B; Tr. 1524–25, 1626–27, 1745, 2276, 2804, 2810.)[90] But the fact that the system may serve the convenience of some of respondents' customers does not mean that it necessarily serves the interests of the plywood consuming public. The plywood customers of respondents who appeared in these hearings are plywood middlemen (brokers and wholesalers) who, essentially, resell to lumber dealers who, in turn, resell to building contractors. These middlemen are terribly concerned about *small* differences in price among competing sellers at any point in time because they operate on narrow margins. They are not concerned, however, about a *substantial,* though uniform phantom freight charge which can be passed on to *their* customers. Note the

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[90] See, however, CX 68 where Willamette officials say that abandonment of a West Coast basis will "enable us to give a clearer, more concise price to our customer." See also CX 149A.

following exchange with one of respondents' "customer" witnesses, a plywood middleman:

> Q. Mr. Vagos, as I understand your testimony, it would not concern you if part of your delivered price consisted of phantom freight as that term is used in CX 200?
> A. What matters is what the competitive price is at the point at which I am quoting it to my customer. What matters is what I am quoting to my customer delivered. What the form is does not matter to me. [83]
> Q. So you wouldn't care if phantom freight was a component of that price?
> A. No, it does not matter. (Tr. 2892-93.)[91]

Moreover, on the subject of "convenience," the experience of nonrespondent MacMillan-Bloedel demonstrates that actual freight can readily be used in price calculations. (Tr. 1100.) Besides, even in respondents' formula method of pricing, actual freight must be calculated since it is paid to the carrier, either by the mill (if prepaid) or by the purchaser (if invoiced freight collect). (See Finding 81.) It is apparent also that respondents rely on actual freight computations to determine the amount of phantom freight or "freight pick-up" in each transaction. (Finding 106.)

126. There was testimony by respondents' officials and plywood middlemen that use of an "index" price plus West Coast freight was simply a matter of form and that price quotations in other "forms," such as a single-figure delivered price without reference to West Coast freight or even F.O.B. prices where the customer arranges transportation from the mill, have been used whenever a customer desires one of these other forms of price quotations. (Tr. 1805, 2033, 2276, 2629, 2887.) The record shows, however, that irrespective of the "form" of the quotation, respondents' basic method of doing business is to take a base price and *add* West Coast freight to arrive at a delivered price. (See Finding 124.) In other words, no matter what the *form* of the transaction, a southern plywood customer simply cannot avoid paying West Coast freight. Thus a Weyerhaeuser customer was told, [84]

> It is quite true that all of us learn something new everyday but it is hardly news that Southern Pine plywood cannot be picked up on a straight F.O.B. mill base to save the West Cost applied freight. This is an equalizer that has been going on in the market for as long as Southern Pine plywood has been manufactured. (CX 113B.)

Similarly, a U.S. Plywood customer asked that it be shipped as follows:

> The material will be shipped F.O.B. mill freight collect. Freight charges are *not* to be added to the invoice, regardless of standard industry practice. (CX 849B.)

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[91] This wholesaler (Vagos) simply puts a margin on top of a mill price and "What really is important is what price our competitors have and if we are working off the same price and if we get the price to get the order, that is important." (Tr. 2913.) Contrast this testimony with the complaint of officials of National Homes who "contend that only actual freight should be charged and not the West Coast applicable rate." (CX 579.)

U.S. Plywood's reaction to this request was "With reference to the FOB mill, freight collect, regardless of standard industry practice I'm sure we are not interested. . . ." (CX 849A.)

Respondents argue, based upon testimony elicited from respondents' officials, that the use of the form of pricing in which West Coast freight is added to a base price has been declining since 1970 because comparisons with the delivered price of fir are no longer as imperative as they were previously, now that fir has been withdrawn from the South. According to respondents, the usefulness of this "form" of pricing is currently confined largely to the "gray" area where fir and pine still compete. (Tr. 1606–07, 1853, 2203, 2276.)

This argument nicely confuses "form" and "substance" and is wrong about both. First, as a matter of "form," the record shows that a base price *plus* West Coast freight is still extensively used throughout the plywood industry. Thus, *Crow's* is obviously reflecting industry practice when it continues to use the West Coast freight formula (Tr. 321, 335, 354); the West Coast freight formula is still used in "PTS" contracts (Findings 76, 94); direct mill sales are made in terms of a base price plus West Coast freight (Findings 78, 93); intra-corporate transfers are in the form of a base price [85] plus West Coast freight (Finding 96); and, in general, prices in the form of a base price plus West Coast freight are still widely used throughout the southern plywood industry. (Tr. 847, 869, 1539, 2202, 2277, 2724.)

In 1973 the form of pricing which added West Coast freight to a base price was so prevalent that Georgia-Pacific described a switch from this method to F.O.B. pricing as a "major change." (CX 808A.) In 1974, Boise Cascade speculated about the implications of a "completely different way of pricing and extending freight from the traditional method." (CX 839B.) Also in 1974, Willamette officials contemplated the significance of discontinuing "our practice of quoting on a West Coast basis or referring to a West Coast basis in any of our quotations or price lists." (CX 68.)

As for the so-called F.O.B. "form" in transactions where the customer arranges transportation, a true F.O.B. price is not used; instead, respondents use a delivered price which includes West Coast freight and allow a small discount. (Findings 120, 121.)

Turning to "substance," it is true that a base price plus West Coast freight can be converted into a simple delivered price. But when this is done in the southern plywood industry, the delivered price includes West Coast freight. (CX 202A; Tr. 717–18, 810–11, 956–57.) In January 1973, counsel for the Federal Trade Commission and counsel for Georgia-Pacific had the following exchange which makes *no* reference to the "form" of the transaction:

> 1. *Question.* Does Georgia-Pacific use and has it used the Coast Rail Freight Rate as the basis for computing delivered prices for shipments of softwood plywood from Southern plants?
>
> *Answer.* Yes, Georgia-Pacific Corporation does use and has used the Rail Freight Rate from the West Coast to Southern delivery points as one factor in determining prices for softwood plywood shipped from its Southern plants.
>
> [86] 2. *Question.* If so, please describe the history of how Georgia-Pacific came to use its method of freight computation.
>
> *Answer.* Before the existence of the Southern softwood plywood industry, plywood supplied to Southern purchasers was manufactured and delivered from West Coast fir plywood plants and obviously contained as one of its delivered price factors rail freight from a West Coast fir plywood plant. The Southern pine plywood industry then had and still does have as a competitor West Coast manufactured fir plywood. Thus, in pricing Southern manufactured pine plywood with its higher inplant manufacturing costs, the delivered price of West Coast plywood became a necessary factor to consider in order to price Southern plywood competitively with West Coast plywood. (CX 487A.)

127. There is no dispute between the experts called by either side — Mr. Glassman (FTC staff economist) and Dr. Steiner (the economist called by respondents) — that it was rational, in a profit maximization sense, for respondents, at the outset of the southern pine industry, to attempt to sell southern yellow pine plywood at the same delivered price as western fir plywood. (Tr. 1228–29, 3622, 4535, 4541.) In fact, Mr. Glassman testified that from the producers' standpoint it was a matter of "economic necessity" ("economic necessity" here meaning profit maximization (Tr. 4535, 4541)) for the two products to be priced at the same level because a southern price below the western price would have created a disincentive to ship fir plywood into the South at a time when the southern pine mills could not possibily produce enough plywood to satisfy southern needs. (Tr. 1228–29.) Mr. Glassman's testimony, however, is fairly read as meaning that it is the function of the market to determine whether the objective of price parity between pine and fir is realized, and he specially denied that this objective is an economically acceptable rationale for use of a distant basing point. (Tr. 1228–29.) [87]

Moreover Mr. Glassman did *not* say that more than 13 years after the formation of the southern pine industry, when southern sheathing production now *exceeds* western sheathing production, there is any necessity for southern mills to arrive at their prices by adding on West Coast freight. While it is true, according to Mr. Glassman, that the price relationships of the two products will tend to be in line (Tr. 1230), respondents have not explained why that "line" cannot be drawn at sharply lower plywood prices — *for both southern and western plywood* — which reflects the enormous new capacity and locational cost advantages of southern mills.

Respondents' retained economist, Dr. Steiner, testified that he would have expected Southern plywood to have found its own independent pricing level by this time, and that the level would approximate the costs, allowing for a fair profit, of the most efficient producer. (Tr. 3625–28.)[92] Instead, southern plywood prices and profits continue to reflect phantom freight from the West Coast (see Findings 132 and 137 for proof of *increasing* southern prices and profits) rather than a trend toward a competitive price as established by the most efficient producer.

Oddly enough, because of phantom freight the most efficient producers in the plywood industry have *lower* profits than the less efficient mills. This is illustrated by the fact that although southern delivered prices are lower than western, the operation of the industry's phantom freight formula, nevertheless, produces higher profits for the southern mills than the more effficient western "sheathing" plywood mills. For example, in 1973 western sheathing was being sold by Georgia-Pacific's [88] western plants producing predominantly sheathing — the most efficient sheathing plants in the industry (Finding 140) — at a net average price of $89.61 per thousand square feet (calculated on the basis of delivered price less actual freight) while southern plywood was being sold at a net average price of $100.03 (*i.e.*, including West Coast freight, less actual freight). (RX 452 *in camera.*) The record shows that at a price of $89.61, Georgia-Pacific was able to realize a substantial profit before taxes on sales of western plywood from its efficient western "sheathing" mills of $23.77. The record shows, however, that a price of $100.03 for southern plywood produced a still higher profit of $26.83. (RX 452 *in camera.*)[93]

128. The rationality of the objective of the southern pine plywood mills — to achieve a southern pine price at or near a western fir price — was further articulated as follows:

> (a) The delivered price of fir plywood (which includes West Coast freight *paid to the railroads*) had established the "value" of the product and respondents were entitled to realize that "value" by use of the West Coast freight factor. (Tr. 1142–44, 1151–52, 1634–35.)
>
> (b) Sale of southern pine plywood at substantially lower prices — say, by using actual freight — would have produced an undesirable result (to the producers), namely, "If we were under the price that somebody else [89] was paying by very

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[92] It is doubtful that further entry into the South will be so significant as to erode prices and profits. The American Plywood Association predicted that "By 1973. . .most really substantial increases in Southern capacity will have been accomplished. From that point on, any additions will be primarily a matter of expanding existing facilities." (RX 10J.) In fact, the prediction has been proven quite accurate. (See RX 11E and CX 138C.)

[93] The profits of Georgia-Pacific's southern plywood mills declined in the deep recession years 1974 and 1975 — in addition to the building recession, there were strikes in southern mills (RX 452 *in camera*; Tr. 4220, 4222–23); it should be noted, however, that except for two years, between the period 1964–1975, Georgia-Pacific's southern mills usually had substantially higher profits per thousand square feet than all of Georgia-Pacific's western mills. (RX 456 *in camera*; see also Tr. 1529–30.)

much, they would just take all of our plywood and that would be the end of it." (Tr. 1754.)

(c) Although freight costs from the South were substantially less than southern rates, there was no cheaper price realistically available in the market. As a Willamette official explained:

> He [the customer in the South] couldn't buy plywood any cheaper from anyone else so there was no reason for us to cut our price. (Tr. 1754.)

(d) As for the substitution of the neatly predictable West Coast rate for the extremely unpredictable southern schedule, it is respondents' view that the plywood business is "competitive enough" without this added complication. (Tr. 2741.)

Price History

129. When southern pine plywood was first sold, respondents used the same base prices as western plywood, and with the addition of West Coast freight arrived at delivered pine prices which were the same as western delivered prices. (CX's 2A–B; Tr. 1003–04, 1421.)[94]

[90] 130. The basic policy of respondents has been to attempt to sell southern plywood at or near the delivered price of western plywood, with the difference between actual freight and West Coast freight, to be taken as an incremental gain for the southern mills. (CX 99V(1); RX's 90A–B; Tr. 1394, 1431, 2203–06, 2210–11, 2216, 2610; Findings 72–73.)

131. Despite the plan of respondents to charge a delivered price for southern plywood which was the same as the delivered price of western plywood, differences in the prices of the two products developed. The record shows the following:

(a) Because southern plywood was perceived at the outset of the industry as inferior in quality to western plywood, southern mills found that it was necessary, shortly after the introduction of pine, to sell the new product at a price which was slightly less than the delivered price of western plywood. (Tr. 953, 1636, 1673, 1753, 1759–60, 2203–04, 2610–11, 2737–40, 2790–91.)

(b) Although southern pine plywood is considered by industry members as equivalent in quality to western fir (Tr. 2832–33), consumer preference for fir has persisted (Tr. 1472, 1676–77, 2873), as have somewhat lower prices for pine plywood during most of the period 1963 to the present. To illustrate, during the period January, 1969 to August, 1971, *Random Lengths* issued 134 reports where a direct comparison can be made between western and southern prices for 1/2 inch 3-ply sheathing. In 13% of the reports, the prices are the same. In 15% of the reports, southern plywood was higher than western (about half the time, a difference of $2 or less). In 72% of the reports, western was higher than southern, but the differences in these reports were within a narrow range: 21% — a $1 difference;

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[94] See also a 1965 report prepared for MacMillan-Bloedel (Tr. 1073–74) which stated:

> Southern Pine Sheathing is sold on a basis of the DELIVERED price of West Coast Sheathing, less actual freight at Southern rail rate to point of destination, less functional discounts of 5/3/2%. (CX 665D.) [Emphasis in original].

51% — a difference of $2 or less; 68% — a [91] difference of $3 or less; 84% — a difference of $4 or less. (RX's 424A–426Z7.)

During the deep recession year 1974, sharper differences were reported. In none of the 50 *Crow's* for this period were western prices cheaper than southern prices, and in only three reports were the two products priced the same. In over half of the reports, the differences range between $4 and $9. (CX's 928A–Z31.)[95] It is significant, however, that even during 1974, and after the massive increase in southern capacity, the prices of the two products tended to be in parity when prices were rising, reflecting presumably an increase in demand and the fact that more plywood was being bought. For example, in the week of March 15, 1974, the price of western plywood rose to $145. (CX 928N.) It remained near that level for the next four weeks when the prices of southern and western were reported as:

Western	*Southern*
150	150
142	140
145	143
145	145

(CX's 928o–Q, 933B)

[92] (c) The prices of western and southern plywood tend to be close in markets where both kinds of plywood are sold in significant quantities. (CX 462D; Tr. 911, 1679–80, 1762–63, 1867, 2212–15.)[96] And while the *exact* same price for fir and pine is uncommon (Tr. 502), a non-respondent producer observed that currently "there is not that much of a difference in price between fir and pine." (Tr. 1099.)

(d) The long range objective of the plywood industry is to abolish all price differences between pine and fir. In the words of one Georgia-Pacific official:

> Certainly, we hope to bring the market together by bringing Pine up rather than Fir down. (CX 571A.)[97]

[93] As for the original reason for the price variation — quality differences — the producers of southern pine plywood have at least attempted to eliminate this source of price differences:

> It is important to note that Southern Pine plywood producers have joined the grading and quality control program of the western producers. Consequently, all

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[95] Whatever differences may have existed in southern and western prices did *not* eliminate the phantom freight or freight "pick-up" which resulted from use of West Coast freight. For example, in 1974 the average reported differential between western and southern 1/2 inch CDX 4–5 ply prices was less than $9.00. (CX's 928A–Z31.) During the same period, the West Coast rates in the most easterly zone ranged between $2.19 and $2.51, which means that the freight charge on southern plywood delivered subject to West Coast freight was between $33.40 and $38.30. (CX 928B, M, Z2.)

[96] Testimony respecting sharply higher prices for fir in the South is largely hypothetical since fir sheathing is no longer an important factor in the South where most southern plywood is sold. (Tr. 1761–62, 1867, 2212.) See also CX's 571A, 573A, and Tr. 1475, 1664–65, 1679–80, which show that outside of its primary marketing area in the South southern pine is sold at prices substantially above the southern plywood prices reported in *Crow's*.

[97] Georgia-Pacific's distribution chief testified, "We may not always hit our objective right but that is our objective, to sell it [Southern Pine] as close to that price of the competitive product." (Tr. 1635; see also Tr. 1679.) The pattern has been that wherever there is an inadequate supply of fir sheathing, the price of pine sheathing approaches the fir price. (Tr. 2886.) Note in this connection that fir production is moving toward the more profitable sanded and specialty items. (Finding 136(a).)

softwood plywoods fly under one flag, as opposed to flags of various competing species. (CX 462i; see also CX 370.)

132. Notwithstanding the massive increase in capacity brought about by the opening of the southern pine industry, there has been no downward trend in plywood prices. In 1974, when the industry "suffered as a consequence of the most severe and prolonged housing depression in history" (RX 11D), the yearly high for 1/2 inch 3-ply sheathing, southern and western, was about $150. (RX's 458A–459B.) This price was substantially higher than the yearly high for either product reported during the period January 1969 to August 1971. (RX's 436–447.)[98] [94]

Entry[99]

133. The profitability of the southern plywood industry (Finding 137) has attracted new mills. In 1969, 34 southern plywood mills were in operation, producing 21 percent of the total plywood produced in the United States that year. By 1974, there were 55 southern mills which accounted for 32.3 percent of total U.S. Plywood production, and 45.7 percent of total sheathing production. (RX's 11E–F, Q.) The record indicates, however, that since 1973 significant new entry has become unlikely.[100]

134. Statistics published by the American Plywood Association indicate that during the period from 1963, when the first southern plywood mills were opened, until 1973, the number of western mills decreased from 157 to 139. During the same time period, the production of softwood plywood, as reported by the American Plywood Association, increased 79 percent from 10.2 billion square feet (3/8 inch basis) to 18.3 billion square feet. Sixty-nine percent of this increase was accounted for by the southern mills which, as indicated above, by 1974 accounted for 32 percent of total industry production. (RX 11E–F.)

135. By the early 1970's southern pine plywood had virtually displaced Douglas fir plywood in the South with some notable exceptions such as sanded plywood which is still made predominantly

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[98] See also CX's 839B, H, and RX 301 for evidence of all-time high plywood prices in 1973 when the early 1970's housing boom was still having an impact. (RX 455B and Tr. 1720, 2247.) For price ranges between 1969 and the first six months of 1974 see RX 301; see also CX 461, p. 48 for price range between 1967 and first six months of 1972.

[99] There is little in the record about the current cost of entry into the plywood industry except that it has gone up precipitously in the last few years. (Tr. 1531–33, 2697.) In order to build its huge Bonner, Montana plywood operation in 1973, it cost U.S. Plywood $114 million for land and timber, plant site, and sawmill. The mill, rated at 300 million feet annual capacity, cost $25 million. (Tr. 2721–22.) A mill in Alabama rated at 120 million feet annual capacity was estimated to cost $11,642,000 to build in 1974. (CX 844C *in camera*.)

[100] See note 92 *supra*.

in the Pacific Northwest. [95] (CX 110W; Tr. 1088–99, 1383, 1762, 2044, 2212, 2792.)[101]

136. The record shows that despite the original apprehension about quality, the difference in price between West Coast plywood and southern plywood led to this acceptance of southern pine plywood. (Finding 131 and Tr. 1438–39, 2793.) Respondents, however, producers in the West as well as the South, have accomplished objectives which are advantageous to them in both geographic areas as a result of the realignment of industry production patterns.

To begin with, this realignment did *not* mean a precipitous drop in the profits of respondents' western mills. In the pre-recession year of 1973, Georgia-Pacific's western mills showed a profit which was more than three times higher than the profits of its western mills at the outset of the southern pine industry in 1964. (RX 456 *in camera.*)[102]

What the realignment does mean is that the southern mills have absorbed the increased demand for sheathing in the South while production in the West of sheathing remains static. (CX 178A; RX 11E.) But stable or even decreased production of sheathing in the West is not unwelcome by respondents considering the raw material problem in that area. Much of the timber supply available to western producers is on public land, unlike the South where an adequate timber supply is owned or leased by the mills. In the period 1970–1975, the amount of available public timber had been sharply reduced and with the withdrawal of millions of acres from commercial use the cost of Douglas fir stumpage had increased by 313 percent. [96] (RX 11L; see also Tr. 1376 ("timber on the West Coast was becoming harder to procure at an economic price, there were vast stands of southern-pine timber available at what appeared to be. . .excellent purchases") as well as Tr. 1384 ("our timber base was shrinking on the West Coast") and Tr. 1424 for contrasting impact in the West and South of bids on forest sale timber.)[103]

Against this background of a shortage of timber and increasing prices in the West, the realignment, when combined with the use of West Coast freight, has accomplished the following:

(a) Respondents' western mills are able to concentrate on high price and high profit specialty items including fully sanded plywood which is not produced in the South.[104] Weyerhaeuser, in fact, anticipated in 1970 that "Sanded plywood which is primarily western Douglas fir should benefit from a shrinking raw material availability." (CX 110Z8 and see Tr. 2208.) Because of the shrinking timber base, Georgia-Pacific has converted its Coos Bay, Oregon mill from a mix of 30% sanded - 70% sheathing to 100% sanded. (Tr. 1385.) The significance of this conversion is manifest. Even in 1973 before the conversion was completed the net profit before taxes of the Coos Bay mill was $36.17 per thousand square feet (CX 483B *in camera*), as compared to $22.83 for all Georgia-Pacific western mills and $26.83 for all Georgia-Pacific southern mills. (RX 456 *in camera.*)

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[101] To this day, the southern mills have not been able to produce a satisfactory fully sanded product because of the wide grain of pine. (Tr. 1378, 1381.) Sanded and specialty products bring a considerably higher return than sheathing. (Tr. 1381.)

[102] In contrast, a large number of worker-owned plywood mills on the West Coast have either been phased out or been acquired by other companies. (Tr. 2723–24.)

[103] For additional evidence respecting western and southern timber supply and prices, see CX 495B; Tr. 1376–77, 1527–28. See also RX 69L for indication that even during the housing depression of 1974, producers of plywood bid up federal timber to extremely high levels underscoring "a strong concern over the prospects for a steady and adequate supply of raw material in the future."

[97] (b) Western sheathing has been withdrawn from the South, but continues to dominate in many Northeast, Central and North Central markets although these markets are closer to southern mills than they are to western mills. (Compare western sheathing distribution in RX 11U with southern sheathing distribution in RX 11Z1.) The record indicates that in areas outside of the South, where fir sheathing predominates, respondents' policy is to resist any erosion of fir prices which might be caused by pine shipments. Thus in 1970, the Georgia-Pacific Minneapolis branch manager reported on a maverick in his area who bases his prices "on Crow's So Pine, where-as this market can demand Crow's West Coast." (CX 545A; see also Finding 131(c).)[105]

(c) Southern sheathing has replaced western sheathing in the South at prices which represent a discount from western base prices to which West Coast freight has been added. This "southern" delivered price, loaded with phantom freight (see note 93, *supra*), produces an impressive level of southern mill profits. (Finding 137.)

137. The entry of new southern mills had led to neither a general downward trend in plywood prices (Finding 132) nor has it affected the profitability of established southern mills. In 1964, Georgia-Pacific's net profit before taxes per thousand square feet of plywood produced in southern mills was $10.40. In the pre-recession years of 1972 and 1973, Georgia-Pacific's profit margin on southern production had risen to $28.49 and $26.83, [98] respectively.[106] A sharp decline of profits in the recession year 1974 (when the building industry collapsed and several southern mills were on strike), was followed by a handsome increase of Georgia-Pacific's southern plywood profits in 1975. (RX 456 *in camera;* Tr. 4220, 4222-23.)

138. Many "entrants" into the southern plywood industry are firms

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[104] See note 101, *supra*.

[105] Note that in 1976, Georgia-Pacific's Minneapolis branch is obtaining the same price for fir and pine. (Tr. 1679.)

[106] As late as 1973 Georgia-Pacific anticipated that the construction of a new southern plywood plant would produce a return on investment after taxes of 16.4 percent, a projected capital recovery period of 4.2 years (estimated cost of plant $11,642,000), net profit before taxes of $31.92 (per thousand square feet) on average net sales of $104.19 (per thousand feet). (CX's 844A, C, E *in camera.*)

Weyerhaeuser's southern plywood mills have been significantly more profitable than its western plywood mills in terms of profit contributions as a percentage of sales. (CX's 897A-926 *in camera.*)

Sheathing, in general, and 2 x 4 studs were the most profitable items sold by Champion in 1972 when measured as a percentage of sales return to manufacturing. (CX 859.)

While Boise's Moncure Mill has had losses (CX's 422A-E *in camera*), its management projected a return on investment before taxes of 34.6 percent in 1973, 48.7 percent in 1974, and 50.5 percent in 1975. (CX 364i *in camera.*) Moncure's losses are attributable to fires, excessive down time due to mechanical failures, a shortage of fuel, labor and management problems. (CX's 364D *in camera*, 814 *in camera;* Tr. 2481, 2505, 2508, 2965.)

with investments in West Coast operations. Respondents, all of whom operate western mills, own 33 of the 55 southern plywood mills in existence in 1974. (Findings 35, 40, 44, 50, 54, 133.)

139. New entrants have been encouraged to follow existing practices. One potential new entrant, Owens-Illinois, was told that Georgia-Pacific would distribute [99] the output of the Owens-Illinois plant on the basis of an agreement which used the West Coast freight formula. (CX's 489A, 601A.)

140. On the basis of this record, I cannot make a conclusive finding with regard to the overall comparative production costs of the southern and western mills. At the opening of the southern plywood industry in 1963, Georgia-Pacific found that it cost no more to produce southern plywood than it did to produce western plywood (Finding 65; see also Tr. 2618–19, 2625–26, for similar experience of Champion, but for evidence of higher southern costs, see Tr. 955, 1036–37, 2737–39.) Moreover Georgia-Pacific anticipated that in the long run it would cost less to produce southern plywood. (RX's 90A–B.) There is also evidence that there is a long run trend toward higher stumpage prices in the West because most of the timber there is on public lands. (Finding 136.) On the other hand, because of certain characteristics of the southern pine species, the production process for southern plywood may have produced some higher costs, particularly in the early stages of the industry. (CX 487A; Tr. 955, 1036–37, 1377–78.)

Complaint counsel introduced evidence showing that the costs of producing most thicknesses of sheathing plywood in the South in 1973 were less than the overall costs in the West. For example, for 1/2 inch CD interior 4 ply with exterior glue, the overall western cost was $114.73 (CX 843, p. 23) as compared to $111.94 in the South. (CX 842, p. 21.)[107] Respondents, relying on the same sources as complaint counsel (American Plywood Association annual cost reports) showed that overall costs in 1974 in the South — $134.11 (RX 449, p. 21) — were higher than in the West — $130.40. (RX 450, p. 13.)[108]

[100] Respondents also introduced evidence that the most efficient sheathing-producing plants are the western plants where 80 percent or more of the production is sheathing, and 20 percent or less is sanded or other plywood products. APA 1974 data shows that costs of these so-called western "sheathing" mills — $119.30 (RX 450, p. 13) — are

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[107] Also, during the entire period 1969–1972, average plywood manufacturing costs were lower in the South than in the West. (CX 838C.)

[108] There are no APA data for the years prior to 1974 showing "sheathing" mills.

substantially lower than the costs of southern mills, all of which produce sheathing mainly.[109] The usefulness of this evidence is diminished, however, because of the exclusion, in the comparison, of all sheathing which is manufactured in the West by so-called "mixed" plants, that is, mills in which production of sheathing is less than 80 percent of the total. As it happens, these so-called mixed mills account for almost half of *total* western production sheathing and therefore the exclusion, according to complaint counsel, makes respondents' comparisons suspect. Respondents, on the other hand, argue that inclusion of the so-called mixed mills (as in the 1973 American Plywood Association data) produces a comparison of western and southern costs which is inherently unreliable because the accounting procedures of the American Plywood Association do not permit proper allocation of certain "green end" and drying costs of mixed mills to sheathing production. (CX's 932A–C.) These conflicting claims of the parties cannot be resolved on the basis of the exhibits and limited testimony respecting comparative costs. Accordingly, I make no general finding on the overall costs of producing western plywood as compared to southern plywood, although there are specific findings relating to costs and profits which are derived from data which does not involve possible discrepancies in APA reporting procedures. (See, for example, Findings 127, 137.) [101]

Other Factors Influencing Plywood Prices

141. The West Coast freight factor has become a focal point for southern yellow pine plywood pricing. (Findings 102–113.) Furthermore, the West Coast rate when combined with "association" weights and common reference to *Crow's* and *Random Lengths* prices has removed a large measure of price uncertainty. (Findings 82, 88, 89–99.) The effects of these practices are to maintain southern prices at an artificially high level reflecting phantom freight, and to keep transactional price variations within a narrow range. (Findings 73–79, 96–99, 110–112, 117–119.)

The record shows, however, that the range of prices, even if it is narrow, is important enough to plywood buyers and sellers, particularly brokers, middlemen, and purchasers for distribution outlets so that they invest time and effort when placing orders in probing the market by telephone for the most favorable transactional price. (Tr. 479–80, 689–90, 871, 1083–84, 1752–53, 1904, 1936–37, 2094–95, 2126–29, 2222–23, 2340, 2482, 2766–67, 2780–81, 2890–92.) Respondents, however, have exaggerated the intensity and scope of this bargaining process, and I specifically reject the notion, advanced by respondents, that plywood is sold in an "auction market" in which, at any point in time, wide variations in prices are the rule rather than the exception. Everyone in the plywood industry knows that negotiations are narrowly circumscribed by *Crow's*, West Coast freight, association weights, and standard discounts. (See Findings 74–112.)[110]

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[109] One major reason for the change was higher glue costs in the South where pine plywood production requires more expensive adhesives. The cost of phenol-based glues rose dramatically in 1974 because of the oil price increase. (RX 11H.)

[102] That *some* bargaining takes place is not in dispute and is shown, for example, by the contracts written on a "PTS" basis which may have the price term expressed as either a small addition or a reduction from *Crow's* or *Random Lengths.* (CX's 79A–F, 90, 195–96, 205B, 209A, 219A–C, 227A, 353 and Finding 110.) As indicated in Findings 92, 110–112, the record shows that the mix of the purchase and the quantity involved influence transactional prices in "PTS" contracts as well as spot sales.

142. The formula used by the southern plywood industry — *Crow's* or *Random Lengths* plus West Coast freight multiplied by association weights — results in fairly predictable prices to direct mill customers and distribution outlets in the freight zones radiating from Portland, Oregon to the East. (Finding 100.) This predictability is subject to distortions, however, to the extent that there are "add-ons" or "up charges" — amounts which are *added* to the delivered price. There was testimony that while all respondents use West Coast freight zones in their direct mill and distribution outlet pricing, they increase, or attempt to increase, the delivered price for sales outside of their primary marketing area by the amount of extra actual freight to the non-primary area. In effect, the use of "add-ons" may produce smaller concentric circles originating at the mills and branches, which are superimposed on the West [103] Coast zones, and could result in prices *above* the level established by adding West Coast freight.

Essentially, "add-ons" are designed to compensate the mills or distribution centers for freight "loss" they would incur if more than primary area actual freight were deducted from the phantom freight as computed from the West Coast. (CX's 112B, 137A–B, 203A–E, 541, 600A–B, 614A–M, 624A; Tr. 860–61, 1546–47, 2041–43, 2712–16.) The significance of "add-ons" is questionable, however, because there is little evidence indicating that sales are made outside of the primary marketing area of the southern mills. (See CX's 356C, 560A.) What the record does show is that all sellers attempt to sell east of the mill (where the West Coast rate increases) but yet as close to the mill as possible to reduce freight "loss" and realize the highest net mill return. (Finding 114.) In sum, there is little evidence of a substantial volume of sales at different prices either to direct mill customers or to distribution outlets within a single West Coast freight zone.[111]

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[110] The fact that plywood producers and dealers as well as trade publications have an overblown view of the competitiveness of the plywood industry is consistent with the Commission's experience with "the rarity with which industry witnesses. . .ever acknowledge the absence of vigorous competition in any form." *British Oxygen Company*, CCH Trade Reg. Rep. 1973–76 Transfer Binder, ¶ 21,063 at p. 20,919 n. 26 (1975) [86 F.T.C. 1241]. Besides, the very testimony cited by respondents in support of the notion of intensive negotiations over price is hedged with caveats. The *Crow's* publisher testified "they will spar *sometimes* between each other" (Tr. 547) and a dealer witness testified "*if* you have a difference of opinion as to what the prevailing price should be" than a counteroffer is made. (Tr. 2931.) Contrast this with the unequivocal testimony of the ex-manager of a Georgia-Pacific branch in Florida, one of the key plywood markets, ("normally your customer knew the cost of that plywood before he ever even called you up, because he also had access to the same costing information that everybody else had" (Tr. 977)).

143. Complaint counsel failed to prove that any of the practices engaged in by respondents — use of West Coast freight, adoption of association weights, and common use of *Crow's* or *Random Lengths* as base prices — has resulted in exactly matching price offers to any customers **[104]** although, as indicated in Findings 92, 110–112, the record shows that differences are usually kept within a narrow range.

144. In addition to the factors cited in Findings 92, 110–112 which create some variation in transactional prices, there are cyclical pressures which influence plywood price levels. (Findings 145–151.)

145. Conditions beyond the control of respondents, such as a change in the number of housing starts (a volatile factor tied to interest rates and the general state of the economy) affect the level of plywood prices. (CX 110G; RX's 13i, 14A–B, 69Z9, Z47–Z48, 83; Tr. 558–59, 1966, 2338, 2785–87, 2871–72.)[112]

146. Weather conditions, boxcar shortages, and strikes also impact on plywood price levels as they affect production and the demand for plywood. (CX's 498, 644A; RX's 69Z1, Z5, 85, 317, 326; Tr. 675, 693, 1422–23, 1425, 2461–62, 2785–87, 2933–34.)

147. As demand changes, the length of the mills' order files (unshipped orders) tends to influence price levels since plywood sellers aim to avoid inventory buildup as well as a situation where there are too many orders. (CX's 326D, E *in camera*, 504B; RX 69R; Tr. 447–48, 1078–79, 1425–26, 1595–97, 2336–37, 2461, 2598.)[113]

[105] 148. Several witnesses testified that respondents have a corporate "philosophy" to operate at full capacity and that this, too, influences price levels. (Tr. 1387, 1602A, 1761, 2207, 2337, 2481, 2567–68, 3009.) But the record shows that this "philosophy" notwithstanding, in slack periods mills are closed down (Tr. 1862, 2337, 2394, 2481, 2744), or production is cut back. (CX 133C, 326E *in camera.*)[114] Weyerhaeuser's overall objective in pricing is —

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[111] Witnesses were asked typically a series of hypothetical questions by respondents' counsel which assumed an opportunity to sell to a nearby customer at one price while another, more distant customer (in the same West Coast freight zone) was "competing" for the same wood. Uniformly, the witnesses testified that they would prefer to sell to the nearby customer and would only sell to the more distant customer if a higher delivered price was offered. (See, *e.g.*, Tr. 1447–48, 1666–67.) In the real world, respondents' sales personnel use a single delivered price for primary markets within a particular West Coast freight zone, and sell most of their plywood to these primary customers at the same price. (See Finding 100.)

[112] A good building year — over 2,000,000 new housing starts — will drive plywood prices up. (Tr. 1423.)

[113] A Champion official testified as follows with respect to the influence of the order file:

> [I]f we have an order for every single quotation that we made, we would shortly have so many orders we wouldn't know what to do with them. So we would have to raise our price to keep the order files from getting into an untenable situation.
>
> Conversely, if we didn't get any orders, we would know our prices are too high and we would have to lower them in search of the market price. (Tr. 2742.)

> To conduct our business in a manner as not to contribute to continued severe pricing declines by forcing production into a weakening market, and to eliminate to the extent possible wild price swings. (CX 896.)[115]

[106] In addition, mills go "off the market" for short periods of time for tactical reasons. (CX's 393, 415o, 853B; RX's 306B, D, E; Tr. 2408.) Moreover, there is other evidence indicating a substantial gap between corporate "philosophy" and practice. For example, in 1974 when a depressed housing market sharply reduced plywood demand, 25 mills closed down and the industry as a whole operated at only 77 percent of capacity. (RX 11K; see also CX 848 for evidence of less than capacity production during part of 1969 and 1970.)[116] On the other hand, complaint counsel presented no evidence showing a systematic adjustment of capacity in order to stabilize prices, and there is evidence that at times excess production may result in a willingness of plywood producers to accept lower prices. (CX 570A; RX 69N.)

149. Some western plywood is sold to brokers or other middlemen who then ship the plywood east in anticipation of a future sale although no actual sale had yet been made. When these so-called "unsold rollers" come to rest at a "diversion" point (or "hit the bumper" in the industry jargon) they must be sold quickly because of high demurrage charges. The existence of these "unsold rollers" may depress plywood price levels (CX 678, p. 11; RX's 69Z36, 309A, 317, 334; Tr. 462–65, 687–88, 874), but unsold "rollers" represent a small proportion of total plywood sales (Tr. 3752)[117] and there is no evidence that a significant amount of southern plywood is sold on such a basis. [107]

150. There is no reliable evidence that speculation in plywood

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[114] The statement of the "philosophy" itself is ambiguous. The Weyerhaeuser official who stated that it was policy to "run it at capacity" immediately added "unless it got too terribly bad we would have to curtail production." (Tr. 2207 and see CX 896 cited in text to this Finding.) By the same token, a U.S. Plywood official who said on direct that his company operates at "optimum production levels" (Tr. 2567) acknowledged on cross that two plants had been recently closed because of the "horrible market." (Tr. 2744.) It is also significant that respondents' overall capacity to produce sheathing, the main product of the southern mills, has been adjusted to the extent that western mills are switching to the production of high-profit sanded and specialty items. (See Finding 136(a).)

[115] For similar policy at Georgia-Pacific, see CX 559C.

[116] Mill shut downs are not confined to slack periods. Even in rising markets, some mills may refuse to quote prices in anticipation of still higher prices in *Crow's* and *Random Lengths*. (See CX 853B.)

[117] See also CX 115, which indicates that the sale of an "isolated distress car" is an exception to the Weyerhaeuser policy of pricing at or above market.

futures on the Chicago Board of Trade affects transactional prices, or has any relevance whatever to the issues raised in this complaint.[118]

151. Complaint counsel failed to prove that plywood prices are maintained at a stable level by reason of any of the practices engaged in by respondents. To the contrary, there is uncontroverted evidence of price fluctuations in both western and southern plywood base prices caused by the cyclical factors discussed in Findings 145–147. The record shows, for example, that the base prices — as reported by *Random Lengths* — could not be maintained at a stable level in the face of a severely depressed building market in 1974–1975. (RX's 69Z4, Z19.) For additional proof that price fluctuations occur regularly see CX 96D; RX's 83, 436–447, 458A–459B.[119] But however often base prices may change the southern plywood industry inevitably adds West Coast freight to the new base prices as reported in *Crow's* and *Random Lengths*. (Findings 72–80, 89–99.)

III

DISCUSSION

Softwood plywood, an essential building material of the housing industry, was manufactured prior to 1963 by respondents and other producers exclusively from the [108] Douglas fir trees grown in or near the Pacific Northwest.[120] This western fir plywood, which still accounts for about 60 percent of plywood production, is sold to buyers located throughout the United States[121] at mill prices to which a substantial freight charge is added in order to arrive at delivered prices.[122] The freight charge from the western mills is the *actual*[123] freight from the Pacific Northwest to eastern freight zones, and is taken from the so-called "West Coast" or Portland, Oregon rail freight rate schedule.[124]

Beginning in 1963, the western plywood producers, led by the industry's largest firm, Georgia-Pacific, entered a new geographic area

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[118] Counsel for respondents informed the administrative law judge that "we don't intend to base our defense in any respect on the existence of the futures contracts." (Tr. 2936.) Notwithstanding this representation, I have examined respondents' proposed findings 179–180 ("The Plywood Futures Market") as well as the material cited therein. Based upon this examination, I have reached the conclusion stated in the text of this Finding.

[119] See also CX 462M, for the following assessment by a Georgia-Pacific official: "There have been dedicated efforts made to control price fluctuation, but little, if any, progress can be claimed. Being a commodity, I fear that our product will continue to suffer from price fluctuations."

[120] Findings 23, 25, 26.

[121] But see Finding 135 with respect to sheathing distribution in the South.

[122] Findings 27, 63, 64.

[123] The freight charge is inflated, however, by the prevalence of "underweights" in western shipments. (Finding 85.) In addition, the "Inland" mills located in Idaho and Montana set their delivered prices on the basis of the higher freight from Portland, Oregon. (See note 30, *supra*.)

[124] Findings 64, 67.

— the South, where vast stands of yellow pine were available for plywood manufacture.[125] The pricing policy followed by respondents in the sale of southern plywood from 1963 to the present is the central point of this case.

According to the complaint, Georgia-Pacific and the four other respondents, whose combined production accounts for over 50 percent of all plywood shipped from southern mills, have followed a practice of refusing to sell at true F.O.B. **[109]** prices; instead, they charge delivered prices for southern plywood which include the West Coast freight rate rather than the actual freight from southern mills to their customers.

Although the complaint at one point describes the challenged practice — the use of West Coast freight in southern shipments — as a "basing point system" (Complaint ¶ 4), in the main charging section ("Nature of the Offense") the term "basing point system" does not appear. There, the offenses charged are a combination or "parallel courses of business behavior" which allegedly establish and maintain "a system of delivered prices based on computation of rail freight from the Pacific Northwest for shipments from mills located outside of that region" (Complaint ¶ 17(a)). The complaint further charges that among the effects of these practices are (1) that prices are stabilized and certainly is provided in the pricing of softwood plywood among competitors (Complaint ¶ 18(a)) and (2) actual and potential competition are reduced and hindered (Complaint ¶ 18(b)).

By its very terms, then, the complaint can be fairly read as covering both a "basing point system," and a system of delivered prices based on concurrent use of an arbitrary freight formula which reduces or hinders price competition. That complaint counsel may have decided not to press one of the two alternative theories pleaded is not prejudicial so long as respondents were apprised of the issues at stake and were given an opportunity to litigate those issues. *ITT Continental Baking Co. Inc.* v. *FTC*, 532 F.2d 207 (2nd Cir. 1976). Clearly respondents were so apprised since at the earliest stage of this proceeding complaint counsel indicated that they would emphasize a price tampering theory, and that absolute price uniformity, the presumed result of a rigid basing point system, was not to be an essential part of complaint counsel's case.[126] **[110]**

Under either theory, however, the main issue raised by the complaint is the same: whether there is a private arrangement arrived at by formal agreement or otherwise, centering around the use of West Coast freight, to affect prices illegally. To put it another way, the ultimate question that must be decided is whether there is a combination or a conspiracy under the Sherman Act to tamper with price by the use of a West Coast freight factor, or if there is no combination, whether the collective, although non-collusive, use of West Coast freight by respondents when shipping from southern mills is a violation of Section 5 of the Federal Trade Commission Act by reason of its impact on prices.

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[125] Finding 26.

[126] See, *e.g.*, Pre-hearing Trial Brief of Complaint Counsel at p. 38 *et seq.* (filed October 14, 1975).

Before turning to the conspiracy issue and the concepts of "agreement" or "meeting of the minds," I believe it is important first to outline the economic effects of the use of the West Coast freight factor. The reason that the usual order of proceeding — that is, starting with the question of "agreement" ("the initial ingredient of a violation of § 1 of the Sherman Act")[127] — has not been followed, is that this case is brought under Section 5 of the Federal Trade Commission Act, and the legality of conduct under that statute need not turn on the Sherman Act concept of "agreement." Besides, in *Container Corporation*, the most recent Supreme Court analysis of price-fixing combinations, the Court seemed much more concerned with the economic consequences of what was done rather than with its ability to infer a combination from certain conduct. As in *Container Corporation*, therefore, it must be determined whether the challenged conduct — here, the use of a West Coast freight factor in the South — reduces or interferes with the setting of prices by free market forces. If any such effects on price occur then an agreement relating to [111] West Coast freight would be *per se* illegal.[128] Furthermore, as indicated later the collective adoption of an arbitrary mechanism affecting price may violate Section 5 of the Federal Trade Commission Act, even in the absence of agreement. Respondents, of course, contend that there is neither an agreement nor collective adoption of an arbitrary pricing device, and that the only influences on plywood prices are the "natural" market phenomena, such as new housing starts, the weather, mill capacities, day-to-day bargaining, and other factors having nothing to do with West Coast freight.

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[127] *United States* v. *Container Corporation*, 393 U.S. 333 at 335 (1968).

[128] *United States* v. *Container Corporation*, 393 U.S. 333 at 337. In the now famous footnote 59 to *United States* v. *Socony-Vacuum Oil Co.*, 310 U.S. 150 at 225 n. 59 (1940), Mr. Justice Douglas writing for the Court said: "But that does not mean that both a purpose and a power to fix prices are necessary for the establishment of a conspiracy under § 1 of the Sherman Act. . .[A] conspiracy to fix prices violates Section 1 of the Act though no overt action is shown, though it is not established that the conspirators had the means available for the accomplishment of their objective, and though the conspiracy embraced but a part of the interstate or foreign commerce in the commodity." This language was clearly dictum since on the facts in *Socony-Vacuum* proof of effect on prices existed. In any event, even assuming a literal reading of footnote 59 may apply to an explicit price-fixing agreement, it is significant that when Mr. Justice Douglas was confronted with the problem of inferring a conspiracy from conduct in *Container Corporation*, he looked to see whether the arrangement operated to limit or reduce price competition. When he found the effects, he said "The limitation or reduction of price competition brings the case within the ban, for as we held in *United States* v. *Socony-Vacuum Oil Co.*, *** n. 59 interference with the setting of price by free market forces is unlawful *per se*." 393 U.S. at 337.

The parties are sharply divided on the facts even to the point where there is a dispute as to whether West Coast freight is actually added or not. On this threshold issue, from my reading of the entire record, I have [112] concluded that respondents do indeed arrive at their price quotations for southern pine plywood by routinely adding West Coast freight to certain base prices.[129]

There is disagreement, too, about most other aspects of southern plywood pricing, but there is little room for argument on the basis of this record about what the use of West Coast freight has not accomplished. Certainly from the largely unexplained and hopelessly disconnected mass of documents that complaint counsel poured into the record, I cannot discern a pattern showing that the use of West Coast freight results in a southern plywood industry which operates as a classic basing point system is supposed to operate: there is no proof in the record of exactly matching delivered price quotes to particular customers; there is no proof that price cutters are "punished" by establishing punitive basing points; and most significantly there is no showing that the industry routinely follows an absolutely uniform base price to which West Coast freight is added, although base prices are usually kept within a narrow ambit of prices appearing in *Crow's* and *Random Lengths*.[130]

It is especially significant that complaint counsel did not call a single customer of respondents or any other plywood producer who could testify about a pattern of matching prices, although complaint counsel were admonished on several occasions that this is the obvious way to prove that the industry operates in such a way that buyers are confronted in the marketplace by identical prices — the presumed result of a traditional basing point system. The total failure to produce evidence on this point, when evidence is readily available, leads to the conclusion that at least on this particular question — exact price uniformity — the evidence would have been adverse to [113] complaint counsel,[131] and consistent with respondents' position that there is no pattern in this industry of precisely matching prices to each customer.

Moreover, not even the economic staff of the Federal Trade Commission could say that the plywood industry functions according to the classic model of a rigid basing point system. The staff economist called by complaint counsel acknowledged that he was not an expert in the plywood industry, and for some unaccountable reason he had not read the record in this case, although the same economist, in his masters dissertation on basing points, had decried the failure of government prosecutors to rely more heavily upon expert economic analysis.[132] I would have expected that if the documents which the government put into the record tend to establish the existence of a traditional basing point system, then this material would have been carefully organized as part of a well-structured economic case. Instead, all that the FTC staff economist did was to present an ABC primer on the way in which a traditional rigid basing point system is supposed to operate (which is hardly in dispute), but he had to concede on cross-examination that he had no knowledge of how close the plywood market actually comes to the academic model he had postulated.

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[129] Findings 72-80, 96-99, 126.

[130] Findings 89-99, 101, 110-112, 143. See Kaysen, *Basing Point Pricing and Public Policy*, Q. J. of Econ., Vol. 63, No. 3 at 289 (Aug. 1949) and Malchup, THE BASING POINT SYSTEM (1949) for discussion of components of a rigid basing point system.

[131] *Cf. Mammoth Oil Co.* v. *United States*, 275 U.S. 13, 52 (1927); *Local 167* v. *United States*, 291 U.S. 293, 296 (1934).

It should also be emphasized that at least one of respondents' objectives (in contrast to the means used to achieve that objective) — a desire to obtain a delivered price for southern pine which approximates the delivered price of Douglas fir — is not the issue in this case. [114] To the contrary, the FTC staff economist indicated that it was rational, in a profit maximization sense, at the start of the southern plywood industry for respondents to attempt to obtain a price for the southern product which was at or near the delivered price of the western product. The FTC staff economist testified that a lower delivered price at the outset of the southern yellow pine industry would have created a disincentive to ship Douglas fir plywood into the areas which might ordinarily be expected to be serviced by the southern mills, but which the southern mills could not adequately supply during the initial phase of their operations.[133]

Respondents' officers offered a more direct explanation for their pricing policy. According to their testimony, the delivered price of Douglas fir plywood had established the market "value" of the product, and therefore, it was proper for the new southern mills to attempt to obtain this "value" although a significant part of the delivered price "value" of western plywood consisted of actual freight from the West Coast which was paid to the railroads and not realized by western mills. That this "freight pick-up" (the industry terminology for excess of phantom over actual freight) could result in an incremental gain in gross margins (while not upsetting the price of western plywood) was undoubtedly a consideration behind the adoption of the West Coast freight formula: obviously, Georgia-Pacific and the other respondents did not go South to depress plywood prices generally or to reduce profits.[134] Still another rational explanation

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[132] See RX 86, p. 67. Respondents' retained expert, on the other hand, decided not to read most of the documentary evidence although it was apparent that these exhibits were the foundation of complaint counsel's case. (Tr. 3715–17.)

[133] Finding 127.

[134] Findings 65–73, 127, 128, 131(d), 132, 137.

(offered by one officer of a respondent company) was that any sharp cut in southern plywood prices, say, by taking the West Coast base price and simply adding on *actual* freight from southern mills, would have produced an apparently undesirable result (to him), namely, "we would sell it out right away. . .if we were under the price that somebody else was paying very much, they would just take all of our plywood and that would be the end of it."[135] [115]

What all these explanations come down to, is that it is not irrational in a profit maximization sense for competitors simultaneously to come to the parallel realization that the long run profits of all firms in an oligopoly setting[136] will suffer if the price for a demand inelastic, undifferentiated product is cut sharply by one firm; therefore, in their own self-interest and in order to maximize profits, all firms attempt to sell the production from a new geographic area at or near the same delivered prices as the old production area, with any saving in freight resulting from locational advantages viewed as a legitimate source of additional profits.[137]

While the objective of the southern policy of the plywood manufacturers is neither obscure nor irrational, this, of course, does not mean that respondents may use any means to accomplish that objective. The assumption of our competitive system is that the market (pressures of supply and demand, including locational advantages of mills), will determine the price at which southern pine plywood is sold, and that *no* aspect of pricing whatever, including the level of prices, or the intensity of price cuts, or the relationship between fir plywood prices and pine plywood prices, or the stability of prices, may be set by a private arrangement among the producers.

As indicated above, from the record I cannot conclude that there was such a private arrangement to maintain a traditional rigid basing point system. Nevertheless, the record shows ample cause for respondents to be motivated toward a price-tampering arrangement aimed at slightly different objectives than precisely matching prices. [116]

In the first place, there was the obvious point that if pine sheathing plywood could be sold in southern markets near the same delivered price as West Coast sheathing, this would be a source of substantial new profits, assuming the price of western sheathing could be maintained outside of the South, or western production was converted to high profit products which could not be readily produced in the South.[138] Additionally, respondents realized that demand would soon build to pass on to buyers the dramatic savings in freight which were at least theoretically possible as a result of the new mill locations.[139] There was apprehension, too, that if building starts declined, the new mills would create excess capacity pressures, and with their high fixed costs they might become a general price depressant instead of a source of additional profits to be derived from the freight advantage.[140] Finally, the success of the southern venture in generating incremental gains to gross margins might be endangered because there existed a substantial problem relating to widely divergent southern freight rates. Shipments east from the Pacific Northwest mills are made to historically neat and concentric eastern freight zones at the same rail rate irrespective of the western shipping point, with the result that the important freight factor in western shipments is exactly predictable.[141] In contrast, the South has a patchwork pattern of widely varied freight rates which differ from mill to mill and from customer location to customer location.[142] Unless doubt about the freight part of southern delivered prices were removed, this, too, might tend to create downward pressure on prices as plywood producers strive to avoid being undersold in a market rife with locational uncertainty. [117]

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[135] Finding 128.

[136] The five respondents control over 50 percent of southern production, with Georgia-Pacific alone having over 30 percent of the market. (Finding 31.) A tight oligopoly has been defined as an industry with a "very small number (eight or fewer) firms supplying 50 percent of the market, with the largest firm having a 20 percent or higher share. . . ." Kaysen and Turner, ANTITRUST POLICY 72 (1959).

[137] Findings 59, 60, 65–73, 127, 128.

By using the West Coast freight factor in quoting prices, respondents accomplished several objectives consistent with achieving the goals and resolving the problems outlined above.

First, the West Coast freight factor served as a focal point for an industry-wide plan to fix the price of southern plywood at or near the same level as the delivered price of western plywood, and thereby allow respondents to take the freight "pick-up" as an incremental gain to gross margins, rather than passing on this locational advantage to buyers.[143] By use of the West Coast freight factor, respondents, in effect, signaled to each other on what to add to base prices and what *not* to cut: they effectively informed each other on where to hold the fort on price competition and thereby keep up the prices of both western and southern plywood.[144] This is borne out by record evidence showing that the West Coast freight factor was given a mantle of invulnerability ("we should not, in any way, endanger this necessary source of income. . .").[145] With uncertainty as to the possibility of deep price cuts to reflect locational advantages removed, competition was limited to small differences in base prices among respondent firms.[146]

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[138] Findings 65–73, 132, 136, 137.

[139] Finding 69.

[140] Finding 70.

[141] Finding 67.

[142] Finding 68.

[143] Findings 65, 69, 73, 102–112.

[144] For a description of focal points as a basis for tacit agreement among oligopolists see Scherer, INDUSTRIAL MARKET STRUCTURE AND ECONOMIC PERFORMANCE 179 (1971). See also *Wall Products Co.* v. *National Gypsum Co.*, 326 F. Supp. 295, 315–16 (N.D. Calif. 1971).

Second, by using the West Coast zones in place of the southern freight rate, respondents immediately eliminated the element of uncertainty in their delivered prices which would have resulted from a diverse freight factor. Combined with the use of still another arbitrary pricing element — association weights — all uncertainty about transportation [118] costs was removed.[147] And with the knowledge that each week's bargaining would at least take into account base prices appearing in *Crow's* or *Random Lengths*, a large measure of price predictability was achieved,[148] although it is plain that cyclical pressures which impact on plywood price stability still persist.[149]

It should be noted that respondents' own explanation for the adoption of the West Coast device is consistent with the proposition that the use of West Coast freight factor minimally has the effect of reducing pricing uncertainty. According to respondents, by using the West Coast rate, the industry is able to produce southern prices which are easily comparable to the orderly western prices as well as making southern prices, themselves, easily comparable.[150] But the fact that in a relatively concentrated industry, the producers arrange to extend an existing formula, which tends to create price predictability, to a new geographic area hardly argues in its favor. To the extent that western prices are in fact certain and predictable, this results from the happenstance[151] of the West Coast freight rate. There is nothing, however, inevitable about transferring the predictability of the *actual* West Coast freight factor to the South. As I indicated earlier, *actual* freight from southern mills varies all over the lot and, undoubtedly, could have produced a great deal of uncertainty with concomitant downward pressure in pricing. Indeed, the mere fact that respondents take it upon themselves to arrange for the arbitrary transfer of the certainty of West Coast rates to the new southern area is strong evidence of intent to remove what could have been a major source of price competition. [119]

Respondents also say that the price for southern pine is a competitive price (presumably set by what the market will bear) because at the outset of the southern plywood industry what the market would bear was the delivered price of western plywood which included West Coast freight.[152] However, in a market where almost all of the important sellers are uniformly quoting prices on the basis of West Coast freight, the "market" has no realistic choice as to what it will or will not bear.[153]

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[145] Finding 103 and see Findings 73–80, 96–112.

[146] Findings 110–112.

[147] Findings 82–88.

[148] Findings 89–101, 110–112.

[149] Finding 151.

[150] Finding 125.

[151] The record is barren as to the historical derivation of the peculiar regularity of the West Coast freight factor.

Moreover, I am not persuaded by respondents' argument that eventually entry (and increased production) will mean that the freight advantage will be passed on, as prices reach the level of costs of the most efficient producers. There is no sign that this has happened in nearly thirteen years of southern production,[154] or that it ever will happen if the industry is left to its own devices. Since "entry" in this instance largely consists of western producers opening southern mills,[155] they "enter" with a built-in incentive not to undercut the western mills by the full extent of the locational advantage. In fact, this is exactly what happened — the western producers all followed the Georgia-Pacific lead and used the West Coast rate to price southern plywood near the level of the western product. Even new (*i.e.*, non-western) producers who may have been induced to enter the South because of the lure of high profits apparently have found very little cause to challenge a West Coast freight system which produces such favorable results for a standardized, price inelastic product in a concentrated industry.[156] Moreover, as indicated in Finding 133, further entry into the southern plywood industry on a [120] scale significant enough to erode prices is unlikely. As for other market conditions which in the long run may tend to drive the southern price down, it is now clear that the most obvious market influence in the pricing of a product for which the transportation cost forms a substantial part of the delivered price — the proximity of mills to users — has been neutralized by the industry-wide adoption of the very arrangement which is the subject of this proceeding.

To sum up, the West Coast freight formula is simply a convenient private arrangement for maintaining southern plywood prices at a level satisfactory to respondents while facilitating the traditional oligopolistic objectives of containing price cutting and limiting price uncertainty. Such a private arrangement is contrary to the assumption of the antitrust laws that the market should determine all aspects of prices, including at what stage locational advantages are asserted and sharp differences in prices may develop. Here, the respondents have adopted a method by which they can interfere with the operation of the market mechanism. When competitors adopt such a formula affecting price, this means that a *private* understanding, centering upon an arbitrary device, is playing a key role, rather than the market itself, in determining whether the objectives of obtaining the same (or nearly the same) price for western and southern plywood and limiting price uncertainty are realized or not. I believe an arrangement of this sort is unlawful whether it is considered as either (1) a conspiracy under the Sherman Act, or (2) an unfair method of competition under Section 5 of the Federal Trade Commission Act.

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[152] Finding 128.
[153] Finding 74.
[154] Finding 127.
[155] Finding 138.
[156] Findings 132, 137, 139.

Turning first to the Sherman Act[157] and the conspiracy issue, it has been the rule since *Interstate Circuit* v. *United States*, 306 U.S. 208 (1939) that when competitors accept (even without previous formal agreement) [121] an invitation to participate in a plan, the necessary consequence of which is restraint of trade, this is enough to establish an unlawful conspiracy or combination.[158] Accordingly, it can be argued that when Georgia-Pacific's West Coast phantom freight formula of quoting prices was assiduously followed by the others, and thereafter all respondents maintained a system of quoting prices which was based on the artificial factor of West Coast phantom freight, this represented a meeting of the minds or, if you will, an illegal tacit agreement in the *Interstate Circuit* sense.

But whatever the ultimate reach of *Interstate Circuit*, clearly it does not mean that *every* action of an industry innovator or leader which is followed in turn by competitors is tantamount to an "invitation" and "acceptance" from which an unlawful *Interstate Circuit* combination can be inferred. In *Theatre Enterprises, Inc.* v. *Paramount Film Distributing Corp.*, 346 U.S. 537 (1954), for example, the Supreme Court held it was not error to deny a directed verdict on a conspiracy charge in circumstances when parallel conduct could readily be explained as the pursuit of individual self-interest without regard to competitor reaction, although it was undisputed that each firm was aware of the action of its competitors. On the other hand, it has been suggested that an *Interstate Circuit* agreement may be inferred if there is evidence of anticompetitive effects flowing from *interdependent* conduct when the action of each firm is made in expectation that others will follow, and the conduct under examination is consistent with the self-interest of each firm only if it is certain that all competitors will do the same.[159]

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[157] Section 1 of the Sherman Act reads as follows:

> Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several states, or with foreign nations, is hereby declared to be illegal. . . .15 U.S.C. § 1 (1964).

[158] See also *American Tobacco Co.* v. *United States*, 328 U.S. 781, 809–10 (1946) ("The essential combination or conspiracy in violation of the Sherman Act may be found in a course of dealing or other circumstances as well as in an exchange of words").

[122] Applying the rationale of "interdependence" to this case, it is possible to infer an *Interstate Circuit* agreement or combination from the fact that no one respondent could expect to sell pine plywood at or near the delivered price for fir plywood unless it were certain that another respondent would not take full advantage of its locational edge, cut pine prices so as to reflect actual freight only, and thereby hope to increase its market share. If, however, combinations are to be inferred solely on the basis of such interdependent calculations, it would mean that practically all pricing decisions in relatively concentrated industries would have conspiratorial overtones, given the fact that when the number of sellers is small, and the demand for a standardized product is inelastic, competitors can scarcely avoid full recognition of their mutual dependence upon each other as they seek to maximize profits at the right price.[160] But whether or not such *mere* interdependence in concentrated markets is an adequate basis for an inference of illegal conspiracy, is a question I do not have to reach on the facts of this case. For here, something extra — a clear signal, a helping hand if you will — was added to the *mechanics* or *process* of interdependent decision-making; namely, by use of the West Coast rate schedule the coordination of oligopolistic decision-making around a convenient focal point was made possible, and the unpredictable element of freight variations inherent in the southern freight rates was removed.

There is ample precedent for the proposition that the use of such private devices to *facilitate* joint profit-maximizing decisions by oligopolists is not permitted under the antitrust laws. In the words of *Cement Institute*, it is the adoption of such "means and measures" and a "handy instrument" to accomplish an otherwise lawful (or at least neutral) result that compels a conclusion that an illegal combination exists.[161] It is especially [123] significant that in *Cement Institute*, the Supreme Court noted that an inference of an *Interstate Circuit* "invitational" conspiracy may arise from the fact that all respondents follow a pricing pattern based on an arbitrary freight basing point.[162]

As for its impact on price certainty, the West Coast freight factor has served a purpose similar to the exchange of price information in *Container Corporation*. As in *Container Corporation*, this is an industry dominated by relatively few sellers of a standardized, price inelastic product, in which traditionally a lower price does not mean a larger share of the available business but a sharing of the existing business at a lower return. Knowing this, the rational plywood producer will naturally seek to avoid competitive price cutting. But if he is uncertain about a key element in his competitors' prices, he will be under pressure to edge downward.[163] The use of the neatly concentric West Coast freight factor in place of the untidy southern rates represents nothing less than an industry arrangement which has been adopted not only as a common rallying point for maintaining southern prices at a level satisfactory to the respondents and for resisting price-cutting pressures, but also to eliminate a large measure of price uncertainty. Even before *Container Corporation*, it was the rule that an inference of conspiracy may be drawn from the use of unnatural pricing formulas involving arbitrary freight rates where nonequidistant sellers were **[124]** able to match their competitors' prices more easily and "eliminate a kind of uncertainty that is a potent force disrupting stable noncompetitive oligopoly pricing."[164]

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[159] See Turner, *The Definition of Agreement Under the Sherman Act: Conscious Parallelism and Refusals To Deal*, 75 Harv. L. Rev. 655, 681 (1962). [hereinafter cited as Turner].

[160] Chamberlain, THE THEORY OF MONOPOLISTIC COMPETITION 46-51 (1965).

[161] *FTC* v. *Cement Institute*, 333 U.S. 683 at 713 (1948).

[162] *Id.* at 716, footnote 17, and accompanying text.

While I have concluded that a Sherman Act rationale of an illegal implied agreement applies in the circumstances described above, my decision does not rest solely on that basis. I believe that concurrent use by respondents of an arbitrary device which may influence price levels or reduce price uncertainty is an unfair method of competition, whether it comes about from an agreement or otherwise. In reaching this conclusion, I start from the proposition that an "agreement" among competitors is summarily proscribed under the antitrust laws because it is a form of private regulation respecting prices and profits which is contrary to our basic economic assumption that the competitive marketplace will control. See, *Northern Pac. Ry.* v. *United States*, 356 U.S. 1, 4–5 (1958); *United States* v. *Trenton Potteries Co.*, 273 U.S. 392, 396–398 (1927). This does not mean, however, that the antitrust policy which condemns agreement can be read as allowing other forms of self-serving arrangements which achieve the same result of substituting for the competitive market private decision-making by presumed rivals. The basic policy of favoring the market as the source of pricing decisions is not so limited as to be concerned merely with agreements, tacit or otherwise.

As it happens, the very purpose of Section 5 of the Federal Trade Commission Act was to implement antitrust policy by eliminating

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[163] Chamberlain, THE THEORY OF MONOPOLISTIC COMPETITION 51–52 (1965). See also Kaysen and Turner, ANTITRUST POLICY 150 (1959) in which the authors describe the function of price uncertainty in concentrated industries as follows:

> But in markets where oligopolistic elements are present, some ignorance and uncertainty about the behavior of rivals is an important competitive element in the market, since it prevents "rational" oligopolistic calculation leading to joint maximization of profits.

[164] Turner, *surpra* note 159 at 674.

every mechanism which may be devised (including devices for working restraints beyond the traditional method of conspiracy) to frustrate competition. See, *FTC* v. *Beech-Nut Packing Co.*, 257 U.S. 441 (1922); *FTC* v. *Brown Shoe Co.*, 384 U.S. 316 (1966); *Atlantic Refining Co.* v. *FTC*, 381 U.S. 357 (1965); *Fashion Originators Guild of America Inc.* v. *FTC*, 312 U.S. 457 (1941). In other words, in applying Section 5, there is no necessity for distinguishing between "agreement" and any other form of [125] artificial pricing mechanism including the concurrent, although *arquendo* non-collusive, adoption by competitors of an artificial formula for quoting prices. This is the plain holding in *Triangle Conduit & Cable Co.* v. *FTC*, 168 F.2d 175 (7th Cir. 1948) *aff'd. by an equally divided Supreme Court sub nom. Clayton Mark & Co.* v. *FTC*, 336 U.S. 956 (1949) where the court sustained Count 2 of a complaint which was based on the "concurrent use of a formula method of making delivered price quotations with the knowledge that each did likewise, with the result that price competition between and among them was unreasonably restrained." 168 F.2d at 176. I believe that *Triangle Conduit* is controlling authority on the question of the legality of artificial formula-pricing under Section 5, irrespective of the existence of a Sherman Act conspiracy. The decision in that case is perfectly consistent with the Supreme Court's treatment of the same question in *Cement Institute:*

> While we hold that the Commission's findings of combination were supported by evidence, that does not mean that existence of a "combination" is an indispensible ingredient of an "unfair method of competition" under the Federal Trade Commission Act.[165]

As for the absence of price uniformity, I do not consider this to be crucial. The mechanism used by the plywood industry is as artificial and as self-serving as an outright agreement in influencing the level of prices, and there is no reason, again, for distinguishing between "agreement" or "device" when it comes to determining the level of uniformity which is required before a violation is found. As indicated earlier, I have concluded that the respondent plywood manufacturers combined to influence the level at which southern plywood was sold by adopting an arbitrary formula which created a pricing focal point and limited price uncertainty. It is of no consequence, [126] therefore, that the practices under consideration did not result in absolute price uniformity, or that certain market factors influencing price levels are beyond respondents' control. The Supreme Court has said that price is so sensitive a barometer of our market economy ("the central nervous system of the economy")[166] that no aspect of pricing can be left to private regulation; accordingly, concerted activity to influence or tamper with the level of prices, directly or indirectly, is as violative of the antitrust laws as one aimed at absolute uniformity. *United States* v. *Container Corp.*, 393 U.S. 333 (1969); *United States* v. *General Motors Corp.*, 384 U.S. 127 (1966); *United States* v. *Socony-Vacuum Oil Co.*, 310 U.S. 150 (1940). As the Supreme Court noted in *Socony-Vacuum*, it is the interference with the *free play* of the market which is the gravamen of the offense:

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[165] *FTC* v. *Cement Institute*, 333 U.S. 683, 721, note 19 (1948).

> Any combination which tampers with price structure is engaged in an unlawful activity. Even though the members of the price-fixing group were in no position to control the market, to the extent that they raised, lowered, or stabilized prices, they would be directly interfering with the free play of market forces. The Act places all such schemes beyond the pale and protects that vital part of our economy against any degree of interference. 310 U.S. at 221.[167]

[127] There is no reason why a different stanadard respecting price uniformity should be applied to parallel adoption of an arbitrary West Coast basing point which influences prices in much the same artificial way as an outright agreement respecting price levels.

On the question of factors influencing price, respondents' retained expert, Dr. Peter Steiner, gave extensive testimony in which he reviewed in detail aspects of plywood marketing which contribute to price uncertainty and instability in the plywood industry. This testimony is substantially consistent with my findings that there may indeed be factors which influence plywood prices (whether they be transactional prices, or the level of prices, or the trend in prices) apart from the West Coast freight factor.[168] But I do not understand that the legality of a practice turns on what respondents did not do, or on what respondents could not control, or on what respondents left untouched after adopting the West Coast formula as a means of keeping prices up and reducing uncertainty in the market. That the industry retains some of the hallmarks of a competitive market is irrelevant, as the Court has plainly indicated in *Socony-Vacuum* and

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[166] *United States* v. *Socony-Vacuum Oil Co.*, 310 U.S. 150, 224 n. 59 (1940).

[167] If the only issue in this case was whether respondents had conspired to charge exactly matching prices, then I would agree with respondents that the language in *Chain Institute* v. *FTC*, 246 F.2d 231 at 239 (8th Cir. 1957) ("If there is competition in base prices there cannot possibly be any 'systematic matching' of delivered prices," language cited by the Court from the Commission's supplemental brief) might be controlling. However, I interpret a complaint alleging the stabilization and reduction of competition to be grounded on *Socony-Vacuum* and its progeny which have held that neither the existence of price variations nor the inability of firms to control the market are crucial. See, *e.g.*, *United States* v. *Gasoline Retailers Ass'n., Inc.*, 285 F.2d 688 (7th Cir. 1961); *Plymouth Dealers' Ass'n. of No. Cal.* v. *United States*, 279 F.2d 128 (9th Cir. 1960); *United States* v. *American Smelting and Refining Co.*, 182 F. Supp. 834 (S.D.N.Y. 1960).

[168] Findings 141-151.

Container Corporation if respondents adopt an arbitrary [128] mechanism which tampers with price in any way.[169] Based on the record evidence, I have concluded that this is precisely what respondents have done. Irrespective of what competition remains, it is clearly illegal for competitors to arrange matters so that any aspect of competition is removed with the result that one can never tell how competitive the market would have been but for the restraint. [129]

Furthermore, on the question of price uniformity, the Commission need not ignore the obvious fact that the plywood industry has, in effect, put into place a system which could easily produce absolute uniformity. The elements of such a system — ready availability of a uniform base price (the prices reported in *Crow's* or *Random Lengths*) plus use of an arbitrary freight factor, as well as so-called "association" weights could produce price uniformity down to the last penny. Moreover, since the record plainly shows that each of these pricing factors has been used by respondents, the dangers inherent in such a threat are very real indeed. Clearly, the Federal Trade Commission has authority to dismantle the illegal parts of this machinery even though absolutely uniform prices have not been obtained. *FTC* v. *Cement Institute*, 333 U.S. 683, 708 (1948).

Confronted with an industry which has already accumulated all of the means which it needs to fix uniform prices, and especially such a highly suspicious mechanism as an arbitrary West Coast freight rate and "association" weights, the Commission need not sit by until total uniformity comes about.[170] Where the facts indicate that the respondents have followed a parallel course of conduct which creates all that is necessary to carry out the conspiracy, particularly the parallel adoption of an artificial pricing element, this is more than an adequate basis for remedial action by the Commission. See, *FTC* v. *Cement Institute*, 333 U.S. 683, 693 (1948). [130]

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[169] The arrangement in *Container Corporation* was stricken down by the Supreme Court although the District Court made findings relating to generally declining prices and the lack of price uniformity as well as the existence of myriad market and competitive factors affecting price. In its decision, the lower court cited the following factors as affecting the prices of each firm: estimates prepared from its internal manual; current plant production load or existence of idle time in its plant, a condition which varies widely in each plant from week to week, season to season, and with the rise and fall of business activity of its customers, suitability of the equipment in its plant for the production of the particular container and the expense of obtaining new equipment when necessary; availability of any special materials needed to produce the order; desirability of adding the particular order to the then scheduled plant production mix and the ability to do so, which varies continuously in the operation of the plant; convenience of customer's plant location for servicing and cost of delivery; size of the order, *e.g.*, carload or less than carload shipment, and customer's prescribed delivery schedule; customer's credit rating; growth prospects of the account and the possibility of substantial future orders; the experimental or developmental character of the particular container and the need to gain manufacturing and marketing experience with respect to it; amount of customer's business represented by the order; general market conditions in the southeastern United States and in the corrugated container industry particularly; prices of its recent sales of the same or other corrugated containers to that customer; customer loyalty; effect of the order on its costs and profits; and prices believed to have been most recently charged or quoted by competitors, when such defendant believes it has sufficient basis for such belief. *United States* v. *Container Corporation of America*, 273 F. Supp. 18, 26 (M.D.N.C.1967).

[170] In *Allied Paper Mills* v. *FTC*, 168 F.2d 600, 606 (7th Cir. 1948), the Circuit Court said that where ". . .the pattern clearly provides a means of fixing uniform prices [respondents'] temporary departure from their system or temporary inability to carry through their purpose does not affect its legality. [Respondents'] degree of success in stifling price competition is not the measure of their liability."

In sum, enough anticompetitive mischief has already been accomplished by respondents and no additional proof of wrongdoing, such as uniform prices or a fixed price level, is necessary. With the opening of the vast stands of southern pine, the consuming public had every reason to expect that at least one significant cost included in the price of a new home — plywood sheathing — would be sharply reduced. The West Coast phantom freight formula was a form of private regulation which the industry adopted to prevent this from happening. This plan succeeded in restricting price competition to a narrow range and in keeping the delivered price of the new southern product pegged near the delivered price of western plywood although the southern mills were practically next door to important building markets in the eastern half of the country. The Commission should dismantle this illegal scheme whether it is characterized as (1) a conspiracy, or as (2) an unfair method of competition which is contrary to the policy of the antitrust laws. For the reasons stated above, the use of West Coast freight in shipments from southern mills violates Section 5 of the Federal Trade Commission Act under either rubric.

IV

RELIEF

On the question of relief, the rule is that the agency is allowed wide discretion so long as the remedial order is reasonably related to the unlawful practices found to exist. *FTC* v. *Mandel Bros., Inc.*, 359 U.S. 385 (1959).

Here, an artificial phantom freight factor not only influences the level of delivered prices but it removes a large degree of price uncertainty. Therefore, an order which eliminates all use of any arbitrary basing point is fully justified. In addition, the order will prohibit reference to "association" weights which are inextricably linked to the use of a West Coast freight factor in arriving at predictable delivered prices. [131]

Under the authority of *FTC* v. *National Lead Co.*, 352 U.S. 419 (1957), the order will include a provision requiring a bona fide F.O.B. option to buyers. Respondents have manipulated the level of delivered prices and created a large measure of price certainty by use of the mechanism of a West Coast freight factor. While the order will not proscribe the individual use of delivered prices (so long as freight is not calculated from an arbitrary base and actual freight is used) what is needed, in the words of *National Lead* is a "breathing spell during which independent pricing might be established without the hang-over of the long-existing pattern of collusion." 352 U.S. 419 at 425. True F.O.B. prices, which allow customer pick-ups when they are economically attractive to a buyer are clearly the most effective way of breaking the current industry pattern of adding West Coast freight to arrive at delivered prices and using artificially inflated "F.O.B." prices which inevitably include West Coast freight. A bona fide F.O.B. price "would reintroduce the kind of uncertainties, as to what price will meet or beat the quotations of competitors, that will restore some measure of competitive pricing."[171]

The order, however, will not prohibit reporting of prices by respondents to *Crow's* and *Random Lengths*, as complaint counsel urge. While it is true that *Crow's* or *Random Lengths* may be used, along with West Coast freight and "association" weights, to arrive at uniform prices, there is no pragmatic way of preventing use of published data. The reporting services have ample industry sources to consult (non-respondent mills, lumber brokers, wholesalers, and other customers of respondents), and nothing of consequence will be accomplished if respondents are foreclosed from reporting prices to those media, except possibly to make it more difficult for these publications to exercise their unchallenged right to report on the facts of plywood marketing. On the basis of this record, where no convincing showing was made by complaint counsel that *Crow's* or *Random Lengths* are manipulated or controlled by respondents, I would not interfere with this right. Besides, neither the transmittal by respondents nor the publication by the reporters of mill [132] prices are the real issues in this case. The heart of the matter is the use of West Coast freight as an inevitable addition to the reported prices.

V

CONCLUSIONS

1. The Federal Trade Commission has jurisdiction over the subject matter of this proceeding and over respondents Boise Cascade Corporation, Champion International Corporation, Georgia-Pacific Corporation, Weyerhaeuser Company and Willamette Industries, Inc.

2. The acts and practices charged in the complaint took place in commerce within the meaning of the Federal Trade Commission Act.

3. While engaged in the sale and distribution of softwood plywood, the respondents, individually, and in combination, are now pursuing and for a number of years have pursued parallel courses of business

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[171] Turner, *supra* note 159 at 676.

behavior constituting unfair methods of competition and unfair acts in commerce. Specifically, respondents, individually, and in combination, have been and are now engaged in the following unfair methods of competition and unfair acts and practices:

(a) establishing and maintaining a system of delivered prices based on computation of rail freight from the Pacific Northwest for shipments made from mills located outside of that region;

(b) establishing and maintaining a system of delivered prices based on computation of rail freight and applying it to shipments made by other modes of transportation;

(c) refusing to permit customers who purchase from southern plants the option of picking up purchases at the plant at true F.O.B. mill prices; and [133]

(d) using the identical schedule of estimated weights as a basis for quoting delivered prices.

4. The capacity, tendency and effects of these practices of respondents are to:

(a) stabilize prices and provide a large degree of certainty in the pricing of softwood plywood among competitors;

(b) inflate the price of softwood plywood to consumers;

(c) reduce and hinder actual and potential competition among respondents in the sale and distribution of softwood plywood;

(d) discourage use of the cheapest and most efficient mode of transportation.

5. The conduct of respondents described above constitutes unfair methods of competition, and unfair acts and practices in commerce in violation of Section 5 of the Federal Trade Commission Act (U.S.C. Title 15, Section 45), as amended.

Accordingly, the following order will be issued:

ORDER

I

DEFINITIONS

For the purposes of this order, the following definitions shall apply:

[134] *"points of origin price"* — a price set by a respondent for a purchase by a customer at a mill or distribution point from which a delivered price is quoted to that customer. The "point of origin price" shall be no greater than the delivered price offered to the customer less the actual transportation costs which would have been incurred by the seller if the sale were made on a delivered price basis.

"delivered price" — a price set by a respondent for a purchase by a

customer which includes the cost of transportation to a designated destination point.

II

It is ordered, That respondents Boise Cascade Corporation, Champion International Corporation, Georgia-Pacific Corporation, Weyerhaeuser Company and Willamette Industries, Inc.; their subsidiaries, any concern controlled by a respondent, including joint ventures; their successors and assigns, and their officers, agents, representatives, and employees, directly or indirectly, through any corporate or other device, individually or in combination, in connection with the sale or distribution of softwood plywood, shall forthwith cease and desist: [135]

1. From using, in any manner whatever, any rate of freight or freight factor other than the actual rate of freight applicable to a given sale or purchase when calculating, negotiating or quoting the delivered price for such sale or purchase.
2. From using, in any manner whatever, any rate of freight or freight factor other than the actual rate of freight applicable to a given intra-corporate transfer when calculating, negotiating or quoting the value to be assigned to such transfer.
3. From using, in any manner whatever, any estimated weights as a basis for arriving at freight charges applicable to a given sale or purchase when calculating, negotiating or quoting the delivered price for such sale or purchase unless such estimates are based upon experience with the actual weight of softwood plywood produced by the mill from which shipment is to be made. Such experience shall be accumulated and updated by representative sampling or by other reasonable methods at least once a year.
4. From using, in any manner whatever, any estimated weights as a basis for arriving at freight charges applicable to a given intra-corporate transfer when calculating, [136] negotiating or quoting the value to be assigned to such transfer unless such estimates are based upon experience with the actual weight of softwood plywood produced by the mill from which shipment is to be made. Such experience shall be accumulated and updated by representative sampling or by other reasonable methods at least once a year.

III

It is further ordered, That when a delivered price is offered by a respondent to a customer for the purchase of softwood plywood in quantities of at least a truckload, that respondent shall also allow such customer the option of obtaining a point of origin price and of arranging or furnishing transportation from the mill from which shipment would have been made had the delivered price been accepted.

IV

It is further ordered, That each respondent shall, when a sale of softwood plywood is made on a delivered price basis and is shipped in truckload or carload quantities by common or contract carriers, state on the invoice the amount of actual freight charged the customer, the common or contract carrier rate from the place of shipment [137] to the customer's destination, the specified estimated weights, if and when used, and the point of origin price.

V

It is further ordered, That each respondent shall notify all persons having sales and policy responsibilities in its organization of the terms of the order and publish same in at least two major trade journals or periodicals twice annually for each of two years from the effective date of this order.

VI

It is further ordered, That each respondent notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent which may affect compliance obligations arising out of the order, such as dissolution, assignment or sale resulting in the emergence of a successor corporation, or the creation or dissolution of subsidiaries or joint ventures.

VII

It is further ordered, That within sixty (60) days after the effective date of this order, each respondent shall file with the Federal Trade Commission a written [138] report setting forth in detail the manner and form of its compliance with this order.

OPINION OF THE COMMISSION

BY DIXON, *Commissioner:*

This matter comes before us on a spirited appeal by respondents from an initial decision finding them guilty of tampering with the price of softwood plywood. The complaint was issued on April 18, 1974, charging respondents, five manufacturers of softwood plywood, with having individually and in combination pursued parallel courses of business behavior alleged to constitute unfair methods of competition and unfair and deceptive acts and practices in violation of Section 5 of the Federal Trade Commission Act (15 U.S.C. 45). [2]

In particular the complaint stated that respondents have (a) established and maintained a system of delivered prices for softwood plywood based upon computation of the freight charge from the Pacific Northwest for shipments made from plywood mills located in the South; (b) established and maintained a system of delivered prices based on computation of rail freight and applied these computations to shipments made by other and cheaper modes of transportation; (c) refused to permit customers the option of purchasing at respondents' southern plywood plants at a true F.O.B. price; and (d) used identical and inaccurate estimated shipping weights as the basis for computing the freight component of delivered price quotations.

The alleged effects of these practices have been to (a) stabilize prices and increase certainty in the pricing of plywood among competitors; (b) reduce and hinder actual and potential competition among respondents in the sale and distribution of plywood; (c) create disincentives to the most efficient location of plywood producing points; (d) create disincentives for customers to locate close to plywood producing points; (e) discourage use of the cheapest and most efficient mode of transporting plywood; (f) discriminate in prices between customers; and (g) deceive customers with respect to freight.

A trial was held before Administrative Law Judge (ALJ) Morton Needelman, who found a violation of Section 5 as charged, although he rejected certain particulars of the complaint. Respondents have taken vigorous exception to the ALJ's initial decision, professing to find it riddled with inconsistencies and lacking in support for the conclusions reached. In our view the initial decision embodies a good deal of thoughtful and independent analysis of a voluminous and not altogether unambiguous trial record. Its alleged inconsistencies, we think, are rather the reflection of a generally successful attempt to characterize a complex pattern of behavior which does not conform neatly to traditional models of guilty, or innocent, commercial conduct. Such nonconformity doubtless accounts for the vehemence with which the opposing parties have been able to insist on the correctness of their respective positions and the illogic of the opposition's. This is a genuinely close and unusual case. [3]

Nevertheless, certain preliminary observations may be ventured without fear of substantial contradiction, subject, of course, to the much more extensive exposition in the initial decision. Plywood is manufactured from Douglas fir (grown mainly in the Pacific

Northwest) and various yellow pine species grown in the South. (I.D. 11).[1] Until 1947 all plywood was produced in the States of Washington and Oregon. Thereafter production began in Idaho, Montana, and Northern California. (I.D. 25) By 1963 technological advances had made possible fabrication of plywood from southern pine, and expansion into the South occurred apace. (I.D. 26) The southern region now includes Maryland, Virginia, North Carolina, South Carolina, Georgia, Florida, Alabama, Mississippi, Arkansas, Louisiana, Texas, and Oklahoma. (I.D. 27) In 1974 the West accounted for 61.4 percent of plywood production and the South for 32.3 percent. (I.D. 27) The South, however, produced 45.7 percent of plywood sheathing, (I.D. 27) the product of concern here, and respondents accounted for more than 50 percent of southern production. (60.09 percent in 1971; 54.22 percent in 1973; I.D. 31)

Plywood has traditionally been purchased on the basis of a "delivered price," consisting of a so-called "mill price" (or "base" or "index" price, See n. 2 *infra.*) plus a freight factor, with deduction of various uniform wholesale discounts as appropriate. (I.D. 63)

Interstate Commerce Commission rail freight rates applicable to western plywood shipments are based upon concentric bands or freight zones running from North to South and radiating eastward. The zones originate with the Portland, Oregon zone, which includes most of the western plywood producing region. As a shipment of plywood travels from West to East it enters progressively higher West Coast freight zones, and applicable freight costs rise correspondingly. Within any given western freight zone, however, freight rates are identical. (I.D. 67) [4]

Freight charges from the West are calculated on the basis of weight, with the same rate per pound applicable regardless of shipment size. When plywood was produced entirely in the West the freight factor added to obtain the delivered price was, roughly speaking, actual rail freight from point of origin. (I.D. 64) The qualification results from the fact that in computing and quoting the freight cost, respondents used a set of uniform "association weights" or "estimated weights" to determine shipment weight. The actual weight of a particular shipment of plywood varies with the amount of moisture retained in the wood, so that identical orders may have different weights and incur different actual shipping costs. Association weights resulted in

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[1] The following abbreviations are used herein:

I.D.	Initial Decision (Finding No.)
I.D. p.	Initial Decision (Page No.)
Tr.	Transcript of Testimony, Page No.
CX	Complaint Counsel's Exhibit No.
RX	Respondents' Exhibit No.

uniform quotation of shipping costs irrespective of the costs actually incurred. (I.D. 84, 85)

When plywood production expanded into the South, southern manufacturers continued to compute delivered prices by adding West Coast freight to a base price[2], although the resulting freight factor obviously diverged sharply from the freight actually applicable to a particular sale.[3] The record indicates that the base price to which West Coast freight was added might, at any given time, vary slightly among competing firms, but it generally fell within a narrow range of the Southern pine plywood price reported by industry reporters *Crow's* and *Random Lengths*. In addition, the record indicates that base prices varied substantially over time, on occasion changing from one hour to the next, though more often persisting for much longer periods. (I.D. p. 52 n. 55; 141–2; 144–151) [5]

When southern pine plywood production began it was viewed as a source of substantial added profits for the plywood companies, owing to the large freight cost savings resulting from greater proximity of southern mills to their customers. The logic of southern expansion as viewed at the time is summarized in a magazine article introduced by respondents describing the reasoning of the President of the earliest and largest entrant, Georgia-Pacific:

> Why was Cheatham so anxious to get into plywood in the South? G–P has found that southern pine plywood for rough uses (e.g., siding) costs no more to produce than its Douglas fir equivalent, and as time passes may cost less. But the big advantage is the saving on freight. It costs $15 to $18 to ship 1000 square feet of standard plywood from the Pacific coast to southeastern cities like Memphis and Atlanta. Freight costs for southern pine plywood, even allowing for its slightly heavier weight per square foot, range from perhaps a third of that down to practically nothing, depending on mill and market location. By pricing its pine plywood competitively with the *delivered* price of Douglas fir plywood, G–P can add the freight saving to its margin. . . . (RX 90; I.D. 65)

Economists testifying for both sides in this case agreed that in its early stages of development, it was consistent with the operation of a competitive market for southern plywood to sell at a price largely determined by the price at which western plywood was sold. (I.D. 127) Western plywood comprised the main part of supply, even within the South, and southern mills were thus able to reap the full pecuniary rewards of their favorable location. From the beginning, however, it was recognized that "[a]s southern plywood output grows, so will the pressure for producers to share at least some of the freight savings with purchasers." (RX 90)

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[2] Respondents contest this characterization, arguing that quotation of West Coast freight was purely a matter of form, and that West Coast freight was simply "backed out of" (subtracted from) a previously determined delivered price to arrive at an "index" price that was comparable to the mill price quoted for western plywood (*i.e.*, buyers trying to decide whether to buy from a western or a southern mill could determine which was cheaper by comparing the western mill price with the southern "index" price, since identical western freight would be added to both). We believe, however, that these contentions are adequately dealt with in the detailed findings of the ALJ and that the textual characterization is consistent with the preponderance of the evidence. (I.D. 72–80; 96–99, 126)

[3] Southern freight rates, unlike western rates, are established on a point to point basis, with freight charges varying from mill to mill and customer to customer. Southern rates also include an incentive structure whereby per-unit costs decrease for that portion of a shipment exceeding a specified weight. (I.D. 68)

As southern production expanded, one would indeed have expected above normal profits resulting from lower freight costs to have been transferred in ever greater proportions from producers to consumers, with southern plywood manufacturers competing more intensely with each other (rather than West Coast mills) for business. The ALJ concluded, however, that respondents' continued use of West Coast freight and association weights in calculating the prices they sought to charge has had the effect of retarding the [6] natural operation of competitive forces, resulting in the stabilization of southern pine plywood prices at higher levels than would otherwise have existed. The ALJ held that this practice could be condemned as an unfair method of competition, violative of Section 5, a practice with the tendency and effect of stabilizing prices, along the lines of the Seventh Circuit's alternative holding in *Triangle Conduit and Cable Co., Inc.* v. *FTC,* 168 F. 2d 175 (7th Cir. 1948), *aff'd. per curiam by an equally divided Court, sub nom., Clayton Mark & Co.* v. *FTC,* 336 U.S. 956 (1949). Alternatively, the ALJ held that the practice could be characterized as a combination on the part of respondents to tamper with one element of price, the freight component, illegal under traditional Sherman Act theory regardless of its effect, see e.g., *United States* v. *Socony-Vacuum Oil Co.,* 310 U.S. 150, 224, n. 59 (1940); *Plymouth Dealers Association of Northern California* v. *United States,* 279 F. 2d 1281 (9th Cir. 1960). Respondents contest these conclusions and our own review of the issues follows.

Evidence of Effects on Prices

Respondents contend that the record lacks evidence to support the ALJ's conclusion that their practices stabilized southern plywood prices. In respondents' view, southern prices are fully competitive and have not been artificially maintained by respondents' common use of West Coast freight. While conceding that some measure of competition may exist in the industry, complaint counsel submit that the challenged practices have nevertheless placed substantial limitations upon it.

The underlying question to which we would, ideally, like to know the response is one which the ALJ not unreasonably refused to allow several witnesses to answer, *i.e.,* "but for respondents' practice of computing prices by means of a formula that included the addition of West Coast freight (based on association weights), would southern plywood prices at any given time have been lower than in fact they were?"[4] Obviously the query is one that by its [7] very nature cannot be answered with total assurance, and the ALJ properly refused to allow non-expert witnesses to tender what would have been no more than sheer speculation. (*e.g.*, Tr. 2820–2821) Nevertheless, if the competitive consequences of the challenged practices are to be evaluated, the question cannot be avoided, or at least we must acknowledge that we are ultimately trying to answer this question no matter what more manageable inquiries we may substitute in its place.[5]

Several sorts of observations may be relevant. Among others are the following: (1) By what method are prices set—can we plausibly infer from the way in which prices are established, including the parties' understanding of what they are doing, that prices are not likely to reach competitive levels?[6] [8] (2) What prices were actually quoted? Can one infer from particular prices quoted, their magnitude, variations, differences between customers or locations that such prices were not competitive? (3) Did the industry realize above-normal profits? Competition should lead to the dissipation of excess profits. Their persistence over time may signal anticompetitive behavior.

The ALJ concluded that the use of West Coast freight exercised a stabilizing influence on southern prices because it eliminated a large measure of the uncertainty facing a plywood seller when quoting prices. (I.D. pp. 117–118) The ALJ further concluded that the use of West Coast freight provided a means by which at least part of the freight advantage enjoyed by southern mills over western mills could be preserved as profit for the southern mills even after the West Coast was no longer a significant source of competition.

As noted earlier the evidence indicates that southern plywood delivered prices were customarily calculated by the addition of West Coast freight to a base price. This base price might vary slightly at any particular time as between different sellers and buyers, and was in some instances the subject of negotiation, but as the ALJ found it would be generally set within a narrow range of the quotations appearing in the industry price reporters, *Crow's* and *Random Lengths*. In the ALJ's view, then, when a particular mill or distribution outlet quoted a price it was aware that competitors might be making slight departures from reported base prices (a source of some uncertainty) but could also be entirely sure that the freight factor being applied by those competitors would be identical, rather than varying in proportion to the substantial differences in actual freight costs which might exist. This assurance would arguably incline sellers throughout the industry to quote higher prices to buyers (and prices which varied with the buyers' distance from the West Coast) than they would have were the possibility open that competitors might be making concessions based upon the actual freight advantages available to them, without reference to a formula price including West Coast freight. The collective result of these individual decisions would be, at any specified time, higher and different price levels than would exist absent use of the uniform freight factor.

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[4] By "lower" we do not mean simply lower for all customers. Elimination of restraints of trade may result in *raising* prices to some purchasers (perhaps those whom it is costlier to supply) while lowering them to others. In a freight intensive industry the reallocation might occur roughly along lines of relative actual freight costs.

[5] Complaint counsel perceive in this line of questioning a "Catch 22" situation in which it cannot be proven that prices would have been lower absent the use of West Coast freight because the very use of West Coast freight precludes the existence of data from a market not using West Coast freight. The point is well taken. The question involved here is, by its nature, not susceptible of definitive proof. That does not mean the inquiry cannot be attempted, and that schemes alleged to stabilize prices are immune from scrutiny. Rather, as with any alleged trade restraint, we must simply decide what were the likely tendency and effect of the practices involved.

[6] The best illustration would be overt conspiracy between competitors, which may or may not raise prices, but is so likely to produce such an effect and constitutes such an extreme departure from the competitive norm that the law prohibits it without further inquiry, *e.g.*, *United States* v. *Socony-Vacuum Oil Co.*, 310 U.S. 150 (1940).

Several respondents dismiss this position as "nonsense." (Champion-Georgia Pacific-Weyerhaeuser Appeal Brief at 33). In their view, the fact that base prices were not identical at any given time indicates that the use of West [9] Coast freight was simply a competitively inconsequential matter of form. Whether bargaining and price concessions occurred with respect to the size of the base price or the size of the freight factor was irrelevant as long as bargaining with respect to the ultimate delivered prices resulted. In respondents' view, presumably, the normal bargaining and variation in pricing which might be expected to result from the fact that different sellers enjoy varying and substantial freight advantages to particular customers did in fact occur, but was reflected in the form of variations in the base (and resulting delivered) price, rather than variations in the nominal freight factor.

Of course, where offering prices are universally established pursuant to a formula which discriminates against buyers based upon their distance from a fixed location far from the actual point(s) of shipment, the fact that random discounts from the formula price are given to some buyers as the result of bargaining and market conditions does not mean that the full discriminatory effect of the formula and its industrywide use is thereby dissipated. Similarly, the fact that at any given time quoted prices vary slightly, or that over time quoted prices vary substantially, does not mean that the general level of those prices is a competitive one. The post-complaint explanations of respondents' counsel are not lightly dismissed, but they are somewhat at variance with documentary and some testimonial evidence as to how respondents themselves understood the role of West Coast freight.

(a) *How Is Price Setting Understood; What Prices Are Quoted*

As the law judge recognized, respondents viewed the West Coast freight factor as more than a matter of form. It was, in practice, added to the base price to arrive at a delivered price for plywood (I.D. 75–76, 78–80), and it was seen by respondents as a source of substantial profit, such profit varying to the extent that West Coast freight differed from freight costs actually incurred by the southern mill. Thus, the record contains numerous detailed discussions and analyses by various sales personnel of so-called "freight pick-up," the difference between western freight and actual freight which would accrue as "an incremental gain for the mill." (CX 99v(1)) Elaborate charts were prepared to show the difference between western freight to numerous points in the South and actual freight from the mill to those points. (I.D. 106)

A 1965 marketing study prepared for prospective entrant MacMillan-Bloedel explains the role of West Coast freight:

> There is no such thing as a fixed FOB Mill Pricelist as we know it. Southern Pine Sheathing is sold on a basis of the DELIVERED price of West Coast Sheathing, [10] less actual freight at Southern rail rate to point of destination, less functional discounts of 5/3/2%. *This means your FOB mill net varies with each of the different rate combinations used to various Market points.* Obviously, the closer you can sell your Sheathing to the producing plant, the greater your freight advantage and net mill value.
>
> The sample average freight rate grid attached gives some idea of how all-important this comparative rate structure is. This grid serves the immediate purpose, but a detailed study, by some reputable Rail Transportation Consultant, should be undertaken as part of our eventual Marketing Plan. (See Appendices II and III for specific rates and $freight advantage/disadvantage.) CX 665D [emphasis added]

Why this concern with western freight and freight pick-up? Why should the difference between western and southern freight have been viewed as in any way a meaningful measure of potential profitability if in fact the inclusion of West Coast freight in southern delivered prices was merely a matter of form?

Respondents argue, and the ALJ agreed, that in the infancy of the southern plywood industry it was reasonable to expect that southern prices would in large measure be determined by prices for western production, which until southern production reached a certain level continued to constitute the major source of supply to the South. Thus, variations in western freight might indeed have represented a reasonable measure of expected variations in price and profit realizations by southern plants.[7]

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[7] Note, however, that the record reflects an early small disparity between southern and western base prices due to the belief of some buyers that western plywood was a superior product. (I.D. 131(a))

[11] The concern for West Coast freight rates and preservation of the inviolability of the freight pick-up, however, persists well after southern producers came to account for the bulk of supply in the South and after one would have expected competition among *southern* producers to have become the overwhelming if not sole determinant of southern plywood prices (*e.g.*, I.D. 135, 126; CX 40B; 41; 91A–Z74; 92A–Z72; 137; 142A; 556, 559A–Z45; 563; 564; 565; 566; 580). If respondents' counsel's explanation of how competition in the southern plywood industry worked is correct, the concern of southern plywood firms for freight pick-up should soon have been abandoned as a futile and time-consuming exercise. If actually-realized delivered prices bore no relation to western freight costs, freight pick-up would be an arbitrary and inaccurate measure of profit, because the profit ostensibly realized on freight advantage would presumably be dissipated in competitive bidding against other *southern* mills enjoying similar actual freight advantages, such competition being expressed, however, according to respondent's view in variations in the *base* price.

The seriousness with which freight pick-up was treated, however, suggests strongly that it was viewed by respondents as an indicator of profit potential or at least relative profit potential as between various alternative shipping destinations.[8] Such a perception could only make sense were respondents able to rely in some measure upon the practice of each other and non-respondent competitors to calculate delivered prices by adding West Coast freight to a base price that would vary within a small range. [12]

It is no answer, we believe, to contend that in calculating freight pick-up southern mills were merely indulging the customary propensity of businesspersons to maximize their profit by charging whatever the market will bear. As the ALJ observed, there existed no realistic choice as to what the market would bear, because the market was determined by the sum of the actions of many sellers relying upon an artificial formula to establish the prices they hoped to realize. To be sure, a seller acting independently is entitled to charge whatever customers will pay, irrespective of the seller's costs. However, but for the common use of West Coast freight by southern producers, there would be no conceivable business reason for any one of them to attempt to measure profit potential in shipping to various destinations by reference to costs of shipping incurred by essentially noncompeting sellers located thousands of miles away.

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[8] Some references to freight pick-up suggest that it was viewed as an *absolute* measure of the added profit to be realized by the southern mill (compared to its western counterpart) by virtue of the southern mill's lower shipping costs. This would seem to make little sense if southern mills were incurring different costs of production.

Freight pick-up would constitute a more realistic *relative* measure of the profit to be realized from shipment by a southern plant to one location as opposed to another, assuming, of course, that delivered prices in the South could be counted upon to vary in some relation to the costs of shipping plywood from the West.

An illustration of the departures from the competitive model wrought by the use of West Coast freight is seen in the sometimes expressed preference of southern mills to ship in an easterly direction, since easterly shipments would go to areas with higher West Coast freight, albeit actual shipping costs were based on distance rather than direction (*e.g.*, CX 9A, 17I, 26B, 561, 566A, 861; Tr. 827–29, 841–42, 861–63). For example, in a 1971 memorandum an official of Georgia-Pacific observed with respect to the southern plywood industry:

> All of our competitors truck to job site or to the dealer at no upcharge over the regular carload price, less the usual discounts. The range over which they will truck depends on market conditions, but appears to be roughly up to 500 miles when there is a freight gain. As you know—this gain can sometimes amount to a considerable sum of money when they run into the most westerly part of the highest freight zone. (CX 566A)

Again we must wonder, why among southern competitors should there be any advantage in shipping into a more expensive West Coast freight zone? The answer as perceived by respondents is that reaching a higher West Coast freight zone meant the opportunity to realize a higher delivered price (and by shipping into the westerly part of the highest [13] freight zone one would incur the minimal actual shipping cost necessary to take advantage of such a price). This could only be the case if in fact the use of western freight in southern pine pricing was more than simply a matter of form.

Similarly, a 1974 freight rate book distributed by Willamette to its mills computes the freight pick-up to be realized from shipments to numerous destinations. The book indicates, for example, a greater mill return to be realized by selling from Willamette's Ruston, Louisiana mill into Atlanta than into Corpus Christi, notwithstanding that actual shipping costs from Ruston were greater to Atlanta. (CX 92P, Z–59) A further corollary of these observations is that changes in West Coast shipping rates relative to southern rates were sometimes viewed as a source of added profit by southern mills (*e.g.*, CX 862A). Again, it does not make sense for a southern mill to view an increase in western freight as a source of added profits when there has been no change in the mill's cost structure relative to southern competitors, unless of course it is believed and understood that use of a formula price will allow the increase in western rates to be passed along in the form of higher delivered prices to the customers of southern mills.

Another indication of anticompetitive effects relied upon by the ALJ was the tendency of a given respondent to quote identical delivered prices to direct mill customers in the southern portions of the same western freight zones (I.D. 100), even though the actual costs of delivering to such customers might vary considerably. Once again, one would not expect in a competitive industry in which western freight played only the formalistic role ascribed to it by respondents that the delivered prices quoted to southern purchasers, should depend upon the western freight zone in which they were located.

Respondents contest the ALJ's finding as to uniformity by manufacturer of quoted prices within the southern portions of West Coast freight zones, but we believe it is amply supported by the preponderance of the evidence. This evidence consists of price lists instructing sales agents as to how to set their prices (*e.g.*, CX 2A, 7, 10, 11, 13, 14, 16, 17, 18, 20, 22, 23, 24, 25, 36B, 88B, 112B, 884H, 114, [14] 886Z–29), invoices evidencing actual identical price realizations within the same West Coast freight zone (*e.g.*, CX 419) as well as testimony of witnesses (*e.g.*, Tr. 711–12, 841, 857; *see* I.D. 100 for additional citations). A similar pattern appears in quotations made for long-term contracts which generally were based upon some variation on the *Crow's* price plus West Coast freight. (I.D. 94)

West Coast freight was also added to a reported base price or a slight variant to determine the price at which plywood was transferred from the mill to sales outlets of respondents (excluding Willamette which was not vertically integrated and Boise Cascade's Moncure mill which used a slight variant of the formula). These outlets were operated as separate profit centers, and the evidence thus indicates that transfer prices charged these profit centers by each company varied according to the West Coast freight zone in which the profit center was located. (I.D. 96) Respondents question the relevance of intra-corporate transfer prices, contending that they bear little relationship to the prices which the transferee sales outlets ultimately charge to purchasers. While it is true, if not a truism, to say that sales outlets would seek to sell their plywood at the market price prevailing at the time of sale, it is no less true that this market price was in some measure a function of the quotations being simultaneously rendered by southern sales outlets. And in pricing their products these sales outlets were trying to recoup the cost of acquiring or replacing their inventory, which in turn varied in relation to the West Coast freight zone in which the outlets were located. (I.D. 98)

(b) *Profit Data*

Complaint counsel did not introduce evidence as to the comparative profitability of southern plywood production versus western plywood production as part of their case in chief, but some data with respect to comparative cost structures and profitability was introduced by respondents in their defense and by complaint counsel in rebuttal. Our own detailed analysis of cost data submitted by the parties is contained in the Appendix to this opinion, supplementing I.D. 140. Our analysis indicates that margins on southern plywood have consistently exceeded those on western plywood, and lends support to the ALJ's conclusion that profitability of southern plywood production has generally exceeded that of western. [15]

The persistence of supra-normal profits over some period of time may signal the existence of anticompetitive conduct, although the existence of such profits is hardly proof positive of unlawful behavior. Increases in demand in a particular region of the country may render production in that area highly profitable, notwithstanding the existence of vigorous competition. However, one would expect the persistence of above-normal profits to act as a signal to others to enter the market, with the eventual result that profits would subside to more normal levels.

Recognizing the uncertainties that are likely to attend the use of profit data as evidence of anticompetitive conduct, and the additional uncertainties as to the particular data introduced in this case, we have placed little reliance upon such data in our disposition of the appeal, although we conclude that the available evidence in no way detracts from, and if anything lends modest support to, our conclusion reached on independent grounds that respondents' challenged conduct has affected plywood prices.

(c) *Other Factors*

Factors in addition to those discussed hereinabove might also be cited in analyzing the likelihood that an industry has been pricing at supra-competitive levels. For example, high concentration (I.D. 33), a wide range of customers (I.D. 34), a fungible product (I.D. 59) and relatively price inelastic demand (I.D. 60), all present here, are conditions conducive to the occurrence of joint, interdependent price stabilizing conduct, *e.g.*, Posner, ***Antitrust Law: An Economic Perspective***, pp. 62ff. By themselves they signify little; in combination with the more direct evidence regarding industry pricing practices cited above they also lend modest support to the conclusion that the conduct challenged has affected competition.

(d) *Summary*

For the foregoing reasons we conclude that the preponderance of the evidence in this case supports the ALJ's determination that the joint use by respondents and others of West Coast freight in calculating the delivered price of plywood sold in the South has had the effect of stabilizing southern plywood prices at levels they would not otherwise have achieved. [16]

In reaching this conclusion we hasten to note that the practice of including West Coast freight in delivered price quotations is only one of many factors affecting the price of southern plywood. Others noted by the ALJ include housing starts (a volatile factor affected by interest rates and the general state of the economy, I.D. 145), weather conditions, boxcar shortages, and strikes (I.D. 146) all of which affect the demand for or supply of plywood and thereby its price. In the face of such formidable and volatile determinants of supply and demand it is not surprising that plywood prices have fluctuated substantially over time. Not even a monopolist would necessarily maintain a fixed price in the face of such extreme shifts in demand.

These considerations do not, however, derogate from the role of West Coast freight as one factor influencing the price of southern plywood and in an anticompetitive fashion. Granting fully respondents' contention that the southern plywood market exhibits some indicia of competitive performance, with numerous buyers soliciting quotations from a variety of sellers and choosing the best, the fact remains that the prices actually realized in this market, as in all markets, are a complex function of the myriad desires not only of buyers, reflected in the prices they offer, but of sellers, reflected in the prices they seek. When firms act in a unified fashion, when they seek to pass on costs imposed uniformly upon all of them, or when they seek to obtain prices established pursuant to an arbitrary pricing formula, it defies common sense to suppose that the sum of these collective actions has no effect on price.[9] In this case the evidence indicates that respondents viewed the [17] difference between West Coast and southern freight as an appropriate measure of the relative profitability of making sales to various destinations. (pp. 9–12 *supra*) As a corollary of this, sales of southern plywood to locations in higher *West Coast* freight zones were viewed as being more profitable than sales to lower freight zones, notwithstanding that actual freight in both instances might be the same. (pp. 12–13 *supra*) Respondents have sought to charge prices reflecting the addition of West Coast freight to a base price, and within the South at least have transferred plywood to their distribution outlets at transfer prices which vary depending upon the West Coast freight zone in which the distribution outlet is located. Such outlets in turn are operated as profit centers, whose sales must bear some relationship to their costs. (p. 14 *supra*)

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[9] An analog to the situation involved here is that in which a regulatory action (*e.g.*, imposition of stringent occupational and health or environmental requirements) imposes added costs throughout an industry. If it believed such action to be unwarranted an industry would no doubt be quick to argue that one of its inevitable effects would be to increase costs to consumers, notwithstanding that the industry might be unconcentrated and demand would remain the same after the regulatory action as before. While a single firm faced with increased costs peculiar to itself cannot pass them on absent monopoly power, where all members of an industry face such increased costs the sum of their efforts to pass on these costs will likely result in some increase in price. This is so even though it may appear to any individual firm (and its agents may so testify under oath in administrative proceedings) that it can and does do no more than meet the prevailing market price.

In light of the foregoing we cannot accept respondents' contention that the southern plywood industry's practice of using West Coast freight was no more than an inconsequential matter of form. The obvious inference to be drawn from the fact that the members of an industry use a formula for computing prices which disfavors particular buyers (in this case those in higher West Coast freight zones) for reasons wholly unrelated to the costs of supplying them, is that customers will end up paying prices inconsistent with a competitive regime.

Characterized in terms of the burden of proof, which respondents protest they are being unjustly forced to shoulder, we believe that evidence produced by complaint counsel, summarized *supra* and in the initial decision, was sufficient to support a *prima facie* inference that the use of West Coast freight affected southern plywood price levels. It was thereafter incumbent upon respondents to adduce evidence that this inference was misguided. With respect to the earliest years of the southern pine plywood industry we think respondents have refuted the inference of anticompetitive pricing, with the argument that the price of *western* plywood (it being the dominant source of southern supply) should naturally have been expected to determine the price for southern production. However, this justification will not wash after the earliest years of the industry, when southern plywood became first the dominant, and later, for some sorts of plywood products, the sole source of southern supply. No longer could southern prices, if set at competitive levels, be expected to vary depending upon the West Coast freight zone of the buyer, as the manner in which they were set by individual firms suggests they did. Respondents [18] have not undermined the force of evidence of non-competitive pricing by showing that in some cases bargaining occurs, price concessions are made, and actually realized prices depart from formula prices, because there is no evidence that such bargaining has led to *systematic* dissipation of the effects of using formula prices which include West Coast freight.[10] Accordingly we believe that complaint counsel have

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[10] Even a price-fixing cartel (which respondents were obviously not) may experience periodic or frequent "cheating" by its members, deviations in realized prices from those which the cartel attempts to set. And many of the basing point cases cited by the parties in their briefs have involved some measure of deviation in realized prices from those that would be expected to result from uniform adherence to the basing point formula, *e.g., Rigid Steel Conduit Ass'n. et al.*, 38 F.T.C. 534, 487 (1944), *aff'd. sub nom. Triangle Conduit and Cable Co., Inc.* v. *FTC* 168 F. 2d 175 (7th Cir. 1948), *aff'd per curiam by an equally divided Court, sub nom. Clayton Mark & Co.* v. *FTC*, 336 U.S. 956 (1949). But evidence of random variations in realized prices from those that would result by rigid adherence to the formula by which offering prices are set is not proof that the formula is economically meaningless, exerting no impact upon prices

(Continued)

met their burden of demonstrating that the use of West Coast freight did indeed exert an anticompetitive impact upon southern plywood pricing.

Legal Analysis

Although the ALJ found no substantial evidence of overt collusion among the parties with respect to price, he concluded that the presence of a combination could nevertheless be inferred from their pursuit of a common course of conduct involving the inclusion of a uniform freight charge based on West Coast freight for plywood shipments from southern mills. [19]

Respondents acknowledge that an agreement by competitors to fix or stabilize even one element of the price of any product would be illegal, *United States* v. *Socony-Vacuum Oil Co.*, 310 U.S. 150, 224 n. 59 (1940), but they contend that here there was no express agreement and that the inference of agreement drawn by the ALJ is without support. In respondents' view, their common course of conduct represented merely the continuation of a method of doing business concededly proper while they operated in the West, and found as well by the ALJ to have been justifiable during their earliest years in the South. Citing the Commission's recent decision in *Great Atlantic & Pacific Tea Company Inc.*, 87 F.T.C. 962, *aff'd.* 557 F. 2d 971 (2d Cir. 1977), respondents contend that an inference of conspiracy may be drawn from parallel business conduct only ". . . if it appeared more to the interest of competitors to adopt different practices." *Independent Iron Works, Inc.* v. *United States Steel Corp.*, 177 F. Supp. 743, 747 (N.D. Cal. 1959), *aff'd.*, 322 F. 2d 656 (9th Cir.), *cert. denied,* 375 U.S. 922 (1963), *cited with approval* at 87 F.T.C. 1068.

This statement, cited by the Commission in the context of an alleged conspiracy between a supplier and its customer, stands in need of substantial clarification in the context [20] of an alleged combination between competing oligopolists. In a perfectly competitive industry, in which competitors expect little advantage from attempting to anticipate the reactions of their rivals to their competitive initiatives the *Independent Iron Works* formulation may be adequate. The perceived self-interest of the atomistic competitor lies in reducing its prices in the direction of its costs, assuming that others will not follow and hoping thereby to secure a larger share of the market and greater

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ultimately realized. The inference that respondents ask us to draw from their defense evidence would necessitate that we disregard contemporaneous documentary evidence as to how they viewed the significance of West Coast freight and conclude instead that they behaved irrationally and unknowledgeably in supposing that West Coast freight and freight pick-up were economically meaningful concepts. We believe such an inference would be unwarranted. Cf. *United States* v. *United States Gypsum Co.*, 333 U.S. 364, 396 (1948).

profits. The fact that over the "long run" such initiatives may be matched by others, sometimes leaving the innovator with the same unsatisfying slice of a smaller pie, is thought not to lead the price-cutting competitor to reconsider its definition of self-interest.

Firms in more concentrated industries are able at times to proceed with greater foresight. Is it truly in the interest of a firm to lower prices if its action will surely be matched by others? Often it is not, and thus it may well not be in the firm's "self-interest," as the term is used in common parlance, to initiate a price cut or refrain from imitating a competitor's price rise. But such *interdependent* self-interested action is obviously not the sort which negates the inference of a conspiracy; to the contrary it may well be evidence of one. As Professor Turner has stated:

> . . .conscious parallelism is not even evidence of agreement unless there are some other facts indicating that the decisions of the alleged conspirators were *interdependent*, that the decisions were consistent with the individual self-interest of those concerned only if they all decided the same way. Turner, *The Definition of Agreement Under The Sherman Act: Conscious Parallelism and Refusals to Deal*, 75 Harv. L. Rev. 655, 658 (1962).

And courts in confronting this problem have similarly implied that the inference of agreement may be drawn if the actions of the defendants would be in their own economic interest only if taken in concert with others. *Harlem River Consumers Cooperative, Inc.* v. *Associated Grocers of Harlem, Inc.*, 408 F. Supp., 1251, 1278 (S.D.N.Y. 1976); *North Penn Oil & Tire Co.* v. *Phillips Petroleum Co.*, 358 F. Supp. 908, 923 (E.D. Pa. 1973). [21]

That test is surely met in this case[11] but it arguably proves too much, as Judge Needelman recognizes (I.D. p. 122) because it would seem to condemn all interdependent pricing that leads to prices that diverge from competitive levels.[12] In Judge Needelman's view, however, it is unnecessary to embrace such an extreme proposition because there is here the presence of an additional factor, the adherence by respondents to a highly *artificial* formula for establishing their prices. [22]

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[11] Why have the respondents in this case sought to charge prices for southern plywood which reflect the inclusion of West Coast freight? Why would a seller of southern plywood, competing with other southern sellers, transfer plywood to its distribution outlets on the basis of transfer prices which include West Coast freight, thereby impelling those profit centers to seek higher prices the farther East they are? Why would a seller of southern plywood have believed that West Coast freight could be at all relevant to the price which might be received for plywood manufactured and shipped from the South? Such behavior could be thought self-interested only upon the assumption that all or most other competitors would engage in it.

[12] It is likely to be the case that anytime a competitor charges prices that differ from those that would result in a competitive market such pricing can be rational only if others are behaving the same way. What seemingly dissuades Professor Turner from finding an unlawful conspiracy under such circumstances is the impossibility of any remedy addressed to conduct short of regulating the prices at which the violators will be allowed to sell. Turner, *supra* at pp. 670–671. While intimating no view on that issue, which is not presented here, we note that the same consideration does not obtain where the basis of the alleged conspiracy is not simply the exaction of non-competitive prices, but the use of an artificial formula to set such prices. In the latter case a remedy may be formulated (excision of the artificial pricing system) which does not do violence to traditional notions of the proper role of government in a free economy. cf. Turner *supra* at pp. 676–677.

Judge Needelman's point is well taken[13] but we cannot ignore the force of respondents' counter that the conduct challenged here did evolve in a justifiable way, and the alleged conspiracy thus results from the *continuation* of such conduct after its original justification had passed. In seeking to infer the reasons for this, some credence must be given respondents' alternative explanation—force of habit.[14]

To be sure, this habit was one which various respondents perceived to serve a useful purpose, hence the scattered documentary references by respondents' agents to the necessity of preserving the freight factor at all costs (*e.g.*, I.D. 103–105), to say nothing of the ubiquitous tables of freight pick-up. (I.D. 106) And respondents' recognition of its advantages has no doubt contributed to the maintenance of their habit as much as the propensity of humankind to do things as they have always been done. Nevertheless, it would constitute something of an extension of the common understanding to infer that a "conspiracy" or an "agreement" was the "most likely" cause of the perpetuation of a commercial habit that arose "innocently" and was not excessively difficult to maintain. [23]

While this extension may well be warranted as a matter of Sherman Act doctrine,[15] we need not reach it for our purposes, because Section Five, with its proscription of "unfair methods of competition," permits a more direct approach to the problem of harmful commercial behavior. Force of habit may explain conduct, and soften the attitude of society toward the actor, but it cannot provide a defense for conduct which loses commercial justification and produces anticompetitive results. The Supreme Court has frequently acknowledged the Commission's authority to proscribe anticompetitive conduct which may not fit within the confines of the Sherman Act, *e.g., FTC* v. *Brown Shoe Co.*, 384 U.S. 316 (1966); *FTC* v. *Motion Picture Advertising Serv. Co.*, 344

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[13] Respondents contend that Judge Needelman's "something extra" (I.D. p. 122) is no more than the allegedly collusive activity itself, *i.e.*, the use of West Coast freight in quoting southern prices. In our view the artificiality of the system is appropriately viewed as the "extra" factor, above and beyond simple joint conduct leading to noncompetitive pricing patterns. We think it eminently reasonable as a matter of law to suppose that an agreement can be more readily inferred from joint use of an artificial formula pricing system than simply from joint quotation of prices that depart from competitive expectations, *e.g., Fort Howard Paper Co., et al.* v. *Federal Trade Commission*, 156 F. 2d 899, 907 (7th Cir. 1946).

[14] An argument no doubt calculated by counsel to appeal to a panel of bureaucrats.

[15] Arguing in favor of the finding of a conspiracy are price-fixing cases which arose out of conduct begun during the New Deal under the imprimatur of the National Industrial Recovery Act. When the NRA was declared unconstitutional the joint activity it had previously condoned was not sufficiently modified to escape antitrust condemnation. *e.g., Fort Howard Paper Co., et al.* v. *Federal Trade Commission*, 156 F. 2d 899, 906 (7th Cir. 1946). This case, however, is slightly more difficult, because it is not clear that what is involved is the *continuation of an agreement* after its legal justification has been abruptly terminated. Rather we are asked to conclude that the continuation of conduct while its commercial justification gradually vanishes and disappears itself constitutes an agreement. Given the availability of an alternative and more direct means of dealing with the problem under Section 5 we need not decide whether the inference of a combination would be proper in this case.

U.S. 392, 394–95 (1953); *FTC* v. *Cement Institute,* 333 U.S. 683, 689–93 (1948), and the Seventh Circuit has previously held that the concurrent although non-collusive adoption by competitors of an artificial method of pricing which restrains competition is unlawful. *Triangle Conduit & Cable Co.* v. *FTC,* 168 F. 2d 175 (7th Cir. 1948), *affd. by an equally divided Supreme Court sub nom. Clayton Mark & Co.* v. *FTC,* 336 U.S. 956 (1949). [24]

The same conclusion is warranted in this case. Respondents' joint use of a system of artificial formula pricing has exerted an anticompetitive effect upon pricing in the market for southern plywood. Respondents originally sought to reap as profit the full freight advantage resulting from location of their plants in the South at a time when the bulk of plywood sold in the South continued to be supplied from the West. To accomplish this they sold the plywood they manufactured in the South on the basis of a base price to which West Coast freight was added, a system which persisted even as southern mills became the principal sources of competition with other southern mills. While disparities between the base prices of southern and western plywood suggest that *full* freight advantage is not realized as profit for southern mills (as opposed to cost savings for consumers), the fact that southern producers have sought to obtain prices that depend upon the West Coast freight zone in which their purchaser is located in reliance upon the industry-wide practice, compels the inference that at least some measure of the freight advantage has been preserved for the industry (rather than returned to consumers) by its use of this system, (pp. 6–17 *supra*).

We must note that our conclusion that Section Five prohibits such conduct depends importantly upon the extreme artificiality of the formula pricing involved in this case. The artificiality of a pricing system is what at once suggests that its results are likely to depart from competitive norms and on the other hand that its use has little redeeming commercial justification, assumptions that are borne out by the record before us. A system of zone delivered pricing involving industry-wide use of freight zones designed to approximate, though not in all instances precisely identifying, actual freight costs would obviously present different problems. There is no occasion here, however, for us to decide how much artificiality is too much, for aside from depending upon the circumstances, it is clear that computation of prices pursuant to a formula which involves addition of a freight factor based upon freight rates from a location thousands of miles distant from the point from which the product is actually shipped is highly artificial within any sense of the word. [25]

Respondents have not objected to the form of order proposed by the

ALJ, assuming, *arguendo*, that a violation is found. The order entered herein will proscribe the use of artificial freight factors in calculating plywood prices for outside sales [Par. II(1)] or intra-corporate transfers [II(2)] and require respondents to offer customers the option of furnishing their own transportation for quantities of plywood in excess of a truckload, at a bona fide point of shipment f.o.b. price (Par. III). As the law judge observed, "[t]rue F.O.B. prices, which allow customer pick-ups when they are economically attractive to a buyer are clearly the most effective way of breaking the current industry pattern of using artificially inflated 'F.O.B.' prices which inevitably include West Coast freight." (I.D. p. 131)

In addition, the order will prohibit use of artificial association weights, [Par. II(3,4)] which were part and parcel of the illegal practice and permitted the standardization of artificial freight factors. (I.D. 88) However, the order will permit use of estimated weights based upon experience with the actual weight of softwood plywood produced by the mill from which a particular plywood shipment is to be made.

Appeal of Boise Cascade

Respondent Boise Cascade, while joining generally the arguments raised by other respondents, has filed a separate appeal contending in addition that at least as of February 1972 it discontinued the use of West Coast freight in computing the price of plywood sold from its Moncure, North Carolina mill. The administrative law judge rejected this contention. Boise's liability was alternatively predicated upon the fact that the DeQuincy, Louisiana mill, operated by Boise and Southern Natural Gas Co. as a joint venture (with each having 50 percent ownership) engaged in the challenged method of pricing. Boise denies liability for the actions of its joint venture.

Assuming *arguendo* that discontinuance of the use of West Coast freight as of 1972 would have warranted dismissal of these proceedings as to Boise, we nevertheless believe that the preponderance of the evidence supports the conclusion that the use of West Coast freight was not in substance abandoned at the Moncure plant. The ALJ concluded that contemporaneous documentary evidence (the desk calendar of the Moncure sales manager, CX 813) indicated that offering [26] prices were arrived at by a process of adding West Coast freight to the price reported in industry reporter *Crow's*. The ALJ's analysis of the desk calendar is contained at I.D. 93(b). In some instances the calendar contains entries reflecting a computation of "Crow's" plus "freight" corresponding to the *Crow's* price plus West Coast freight for the applicable date and wood size (*e.g.*, CX 813 Z11). Below this column appear prices for the various zones into which Boise

Cascade made its sales. The ALJ found that prices for Zone A, that nearest to the Moncure plant, were identical to the corresponding "Crow's plus freight" around 40 percent of the time, and within a close range of the rest. Boise suggests that the coincidence of its Zone A prices with the formula price, as well as its sales manager's evident concern with the formula price in formulating Boise zone prices reflects at most consideration of the *competition* rather than any independent use of West Coast freight in arriving at Boise's own prices.[16] Further support for the significance of the calendar entries, however, is supplied by CX 839B, in which Boise officials characterized the effect of a possible consent settlement of the pending charges: [27]

> We will have to comply with an FTC order that dictates a completely different way of pricing and extending freight from the traditional method. (CX 839B)[17]

On balance we believe that the preponderance of the evidence supports the conclusion that the Moncure plant continued to use the challenged method of pricing following 1972.

In addition, there can be little doubt that Boise Southern, Boise's 50 percent owned joint venture continuously engaged in the challenged practice of calculating the price of southern plywood by means of the addition of West Coast freight. (I.D. 78(b)) We believe that for the reasons set forth by the ALJ at I.D. 41 Boise is properly held liable for the plywood pricing practices of this joint venture. Accordingly we must deny its separate appeal.

Except as noted herein, the initial decision of the administrative law judge is sustained and adopted as that of the Commission,[18] and an appropriate order is appended.

APPENDIX

Costs and Profitability of Southern vs. Western Plywood Production

Economic theory suggests that in a competitive industry prices will be driven toward the level of costs, with costs defined to include a return on capital just sufficient to ensure that capital is not diverted to alternative uses. Southern plywood producers initially realized substantial cost advantages by virtue of their greater proximity to sources of demand. While western plywood continued to comprise the bulk of supply it was reasonable for the freight cost savings achieved by southern mills to accrue as profit. As southern production expanded, however, one would expect this profit to be dissipated by the forces of competition, with the freight cost savings resulting from southern production being transferred in ever greater proportions from consumers to producers.

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[16] While on balance we must reject this contention, we note that it is not inherently unreasonable. And what it suggests is that it was hardly necessary for *every* producer in the southern plywood industry to include West Coast freight in its delivered prices in order for the challenged system to have effect, (although the ALJ found that with one major exception respondents' practice was followed by their smaller non-respondent competitors, I.D. 74). So long as the major producers used the system it obviously behooved others to take account of it, or go along with it, in making their own competitive decisions. Boise's evident degree of concern, however, appears a bit too great for us to conclude that it was doing no more than gathering information about the way in which everyone, except for itself, was behaving.

[17] Boise objects to the use of "settlement related" documents where no settlement was reached. It would certainly be improper to use the fact that a settlement was attempted as evidence of any sort that a violation occurred. That is not our purpose in citing CX 839. Rather the document is cited as wholly proper evidence of how Boise understood and characterized its own system of pricing in effect as of 1974. Were Boise's description of its post 1971 system in this appeal an accurate one it is hard to see how it could have viewed any settlement of these charges as imposing "a completely different way of pricing and extending freight" in 1974.

[18] Complaint counsel urged at oral argument that we change "pounds" to "square feet" in I.D. 88, and "delivered price" to "price" in subparagraphs II(1) and II(3) of the order. We hereby accede to these requests.

One way to approach the problem of whether the expected competitive effects have occurred is to compare the relative profitability of presumptively competitive western mills with southern mills, a task well begun by considering relative production costs in the two regions. It is apparent that when they entered the South, plywood companies believed that production costs in the new region would be roughly comparable to those in the old, and that they could thus realize additional profits corresponding to the advantage in freight available from the new location. A magazine article introduced into evidence by respondents (RX 90) described the reasoning of Georgia-Pacific's President:

> "Why was Cheatham so anxious to get into plywood in the South? G-P has found that southern pine plywood for rough uses (*e.g.*, siding) costs no more to produce than its Douglas fir equivalent, and as time passes may cost less. But the big advantage is the saving on freight. It costs $15 to $18 to ship 1000 square feet of standard plywood from the Pacific coast to southeastern cities like Memphis and Atlanta. Freight costs for southern pine plywood, even allowing for its slightly heavier weight per square foot, range from perhaps a third of that down to practically nothing, depending on mill and market location. By pricing its pine plywood [2] competitively with the *delivered* price of Douglas fir plywood, G-P can add the freight saving to its margin. . . ."[1]

The parties are at odds as to whether Georgia-Pacific's original assumption regarding equivalence of production costs was correct, and the Administrative Law Judge declined to make a firm finding on this point. (I.D. 140) Our own review of the record, however, suggests the conclusion that production costs of southern and western sheathing have generally fallen within close range of each other.

The most comprehensive cost statistics available are those published by the American Plywood Association (APA). The record contains APA's annual cost reports for the Southern and Western plywood industries for 1973 and 1974, as well as a chart prepared by Boise Cascade reflecting APA survey data for 1968–1972 (CX 838c) The 1973 reports reveal the following costs for so-called "CDX" plywood (a panel of C and D grade veneers with exterior glue line), the most common form of sheathing plywood:

Thickness	*Costs per 1000 Sq. Ft.*	
	South	*West Coast*
5/16"	$ 75.80	$ 72.61
3/8"	83.52	85.75
1/2" (4 ply)	111.94	114.73
5/8"	140.08	143.30
3/4"	169.77	168.31

(CX 842, p. 21; CX 843, p. 23) [3]

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[1] The article later notes, in keeping with traditional theory, that "As southern plywood output grows, so will the pressure for producers to share at least some of the freight savings with purchasers." The real issue in this case is whether or not an industry practice, whether maintained by design or habit, has impeded the natural operation of competitive pressures.

The 1974 reports reveal the following costs for the same products:

5/16"	$ 89.18	$ 85.83
3/8"	100.00	96.97
1/2" (4 ply)	134.11	130.40
5/8"	166.94	162.17
3/4"	197.41	191.63

(RX 449, p. 21; RX 450, p. 24)

The Boise summary of APA cost data reflects southern costs on average lower than western for 1969–72, and slightly higher in 1968 (CX 838c).

Respondents object to citation of the above western figures, contending that a more appropriate comparison is between the southern mills surveyed by APA and so-called western sheathing mills, *i.e.*, western mills whose production consists almost entirely of sheathing. The southern mills surveyed by APA consist entirely of sheathing mills, while the western mills surveyed included both sheathing mills and so-called "mixed" mills, those producing both sanded and sheathing products. In 1974, however, APA for the first time included figures for western sheathing mills in addition to figures for the entire sample. The record does reflect that these western sheathing mills are somewhat more efficient than southern mills[2] but like the law judge we believe the comparison is of only limited utility. The APA surveys are designed to determine the cost of producing sheathing by region, *regardless of the type of plant producing the sheathing.* Most southern sheathing [4] production occurs in sheathing plants; in the West, however, perhaps half of all sheathing is produced by mixed plants, (*e.g.*, Tr. 4126 "over 50 per cent") and it is, therefore, entirely proper for a cost survey to include a sampling of such mixed plants. (See also Tr. 4119 ff.)[3]

While recognizing the propriety of including both mixed mill and sheathing mill costs in a sampling of western sheathing costs, the ALJ appears to have stopped short of drawing any conclusion on comparative costs because in calculating the cost of sheathing produced by mixed mills "the accounting procedures of the American Plywood Association do not permit proper allocation of certain 'green end' and drying costs to sheathing production. (CX's 932A–C)" This results because industry-wide average green end and drying costs for particular products are figured on the basis of average costs incurred by the reporting plants for all veneers processed, regardless of their end use. Since so-called "A" veneers are not used in sheathing, inclusion of green end and drying costs for these veneers in the averages may distort the overall figures. (I.D. p. 100) [5]

From our review of the relevant figures, however, it appears that even if misallocations of green end and drying costs have occurred, they could not be of a magnitude sufficient to disturb the conclusion of substantial similarity of inter-regional sheathing costs. Thus, the 1974 APA Western Report (RX 450) indicates that for 1/2"

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[2] For example, the cost of producing 1/2" CDX 4 ply incurred by western sheathing plants in the sample was $119.30 (RX 450, p. 13) vs. the above-mentioned southern cost of $130.40. We observe, however, that the figures for 1974 may overstate the disparity between southern and western sheathing plants. *Compare* RX 452 (*in camera*) covering Georgia-Pacific sheathing plants, which reflects a western sheathing plant cost advantage of $12.81 in 1974 but only $7.18 in 1973 and $5.74 in 1975.

[3] The ALJ made this point we think quite convincingly in an extended colloquy with respondents' counsel during voir dire of an APA representative called to authenticate the APA cost studies. (Tr. 4103ff). The bottom line from respondents' point of view was apparently not so much that APA figures are inaccurate measures of average sheathing costs within the South and West, but that these averages were not relevant to complaint counsel's effort to utilize the testimony of respondents' expert, Dr. Steiner, to the government's advantage. Dr. Steiner had testified that over time one would expect prices to approach the marginal costs of the *most efficient* producers. (Tr. 4108)

CDX, 4 ply sheathing the average drying cost assigned to all sheathing is $8.56 while at the more efficient sheathing plants it is $8.28.[4] For green end costs the average for sheathing plants actually exceeds the quoted industry average ($9.80 vs. $9.48). In either event it is hard to see how a more precise allocation of these cost components for mixed plants would have significantly altered the observed relation between total western and southern producing costs cited above.

With respect to wood costs, which are a major component of total cost and a major source of the cost difference observed between sheathing and mixed mills in the West, the APA survey in fact does distinguish between costs of so-called "A" veneers and costs of the less expensive B, C, and D veneers used in sheathing. (CX 932B; Tr. 4255, 4099). The assignment of higher wood costs to sheathing production at mixed mills than to sheathing production at sheathing mills thus appears to reflect actual cost differences incurred in producing sheathing by the mills.[5] For these reasons then, we conclude that the APA studies may properly be used to compare relative production costs for sheathing in the South and West, and those studies indicate that production costs have fallen within a close range of each other during the several years preceding issuance of the complaint in this matter (a few dollars per thousand square feet). **[6]**

While southern and western sheathing *costs* have fallen within close range of each other, the record indicates that the mill net return per unit of plywood has been significantly higher for southern mills than for their western counterparts. Reported *base* prices for southern plywood have generally fallen below base prices for western plywood (I.D. 131), but the addition of western freight to those southern base prices, when only southern freight is being paid, results in a substantially higher return to the southern mill. (The western mill pays actual western freight, so the return to the western mill is measured simply by its base price.)

The ALJ's findings with respect to pricing patterns are contained in I.D. 131. He notes that from January 1969, to August 1971, *Random Lengths* issued 134 reports in which a direct comparison can be made between western and southern prices for 1/2 inch 3-ply sheathing. In 28 percent of the reports southern prices were the same as or lower than western. In the remaining 72 percent of reports wherein western base prices exceeded southern, the reported differences were $4 or less in 84 percent of the cases. $4 would, of course, be far less than the "freight pick-up" or differential between western freight which was added to those southern base prices, and southern freight actually paid. (*e.g.*, CX 91; see n. 6 *infra*)

For 1974 the ALJ found more significant differentials between southern and western base prices, but even in this year, the average reported differential between western and southern 1/2 inch CDX 4–5 ply prices was less than $9. (I.D. p. 91, n. 95) This compares with average freight pick-ups for southern mills in the vicinity of $19 or more.[6]

[7] The foregoing suggests that southern mills have generally realized higher net returns per unit of sales than their western counterparts, which is consistent with evidence to the same effect cited by the ALJ, as well as with evidence of generally, though not uniformly, higher profit margins for southern producers. (CX 127, 137)

Having made the foregoing observations we hasten to add that in our view they constitute no more than modest support for the conclusions that we believe are justified independently by the discussion in the body of our opinion and the initial decision. Aside from numerous uncertainties and inadequacies in the cost and profit information available in this record, it is obvious that supra-normal profitability can readily result from factors other than anticompetitive conduct, for example, unusual growth in a region in which the profits are realized and resultant supra-normal demand. As respondents point out, the issue is not so much whether profits at any given time are above average as whether such above-average profits attract new entry in response, though, of course, such new entry would be expected at some point to result in dissipation of the profits that induced it.

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[4] This figure presumably is properly allocated.

[5] Reasons why wood costs for sheathing are higher at mixed mills than at sheathing mills are suggested by the testimony of Mr. Ridgway at pp. 4097–4098.

[6] The association weight of CDX 1/2 inch 4–5 ply is 1525 pounds (CX 928). Assuming an average freight pick-up of $1.25 per hundred pounds which the record indicates is a reasonable estimate (*e.g.*, CX 137A; 92) the freight pick-up for 1000 square feet of CDX 1/2 inch 4–5 ply would be $19.06. This $19 freight pick-up accruing to the southern mill far more than offsets the average of less than $9 by which western base prices exceeded southern base prices in 1974, to say nothing of the much lower amounts by which western base prices exceeded southern base prices in the 1969–71 period surveyed by the ALJ.

FINAL ORDER

This matter has been heard by the Commission upon the appeal of respondents' counsel from the initial decision and upon briefs and oral argument in support thereof and opposition thereto, and the Commission, for the reasons stated in the accompanying Opinion, has denied the appeal.

It is ordered, That pages 1-132 of the initial decision of the administrative law judge are hereby adopted as the Findings of Fact and Conclusions of Law of the Commission, to the extent not inconsistent with the accompanying Opinion. Other Findings of Fact and Conclusions of Law of the Commission are contained in the accompanying Opinion. [2]

It is further ordered, That the following order to cease and desist be hereby entered:

ORDER

I

DEFINITIONS

For the purposes of this order, the following definitions shall apply:

"point of origin price" — a price set by a respondent for a purchase by a customer at a mill or distribution point from which a delivered price is quoted to that customer. The "point of origin price" shall be no greater than the delivered price offered to the customer less the actual transportation costs which would have been incurred by the seller if the sale were made on a delivered price basis.

"delivered price" — a price set by a respondent for a purchase by a customer which includes the cost of transportation to a designated destination point.

II

It is ordered, That respondents Boise Cascade Corporation, Champion International Corporation, Georgia-Pacific Corporation, Weyerhaeuser Company and Willamette Industries, Inc.; their subsidiaries, any concern controlled by a respondent, including joint ventures; their successors and assigns, and their officers, agents, representatives, and employees, directly or indirectly, through any corporate or other device, individually or in combination, in connection with the sale or distribution of softwood plywood, shall forthwith cease and desist:

1. From using, in any manner whatever, any rate of freight or freight factor other than the actual rate of freight applicable to a given sale or purchase when calculating, negotiating or quoting the price for such sale or purchase.

2. From using, in any manner whatever, any rate of freight or freight factor other than the actual rate of freight applicable to a given intra-corporate transfer when calculating, negotiating or quoting the value to be assigned to such transfer. [3]

3. From using, in any manner whatever, any estimated weights as a basis for arriving at freight charges applicable to a given sale or purchase when calculating, negotiating or quoting the price for such sale or purchase unless such estimates are based upon experience with the actual weight of softwood plywood produced by the mill from which shipment is to be made. Such experience shall be accumulated and updated by representative sampling or by other reasonable methods at least once a year.

4. From using, in any manner whatever, any estimated weights as a basis for arriving at freight charges applicable to a given intra-corporate transfer when calculating, negotiating or quoting the value to be assigned to such transfer unless such estimates are based upon experience with the actual weight of softwood plywood produced by the mill from which shipment is to be made. Such experience shall be accumulated and updated by representative sampling or by other reasonable methods at least once a year.

III

It is further ordered, That when a delivered price is offered by a respondent to a customer for the purchase of softwood plywood in quantities of at least a truckload, that respondent shall also allow such customer the option of obtaining a point of origin price and of arranging or furnishing transportation from the mill from which shipment would have been made had the delivered price been accepted.

IV

It is further ordered, That each respondent shall, when a sale of softwood plywood is made on a delivered price basis and is shipped in truckload or carload quantities by common or contract carriers, state on the invoice the amount of actual freight charged the customer, the common or contract carrier rate from the place of shipment to the customer's destination, the specified estimated weights, if and when used, and the point of origin price. [4]

V

It is further ordered, That each respondent shall notify all persons having sales and policy responsibilities in its organization of the terms of the order and publish same in at least two major trade journals or periodicals twice annually for each of two years from the effective date of this order.

VI

It is further ordered, That each respondent notify the Commission at least thirty (30) days prior to any proposed change in said respondent which may affect compliance obligations arising out of the order, such as dissolution, assignment or sale resulting in the emergence of a successor corporation, or the creation or dissolution of subsidiaries or joint ventures.

VII

It is further ordered, That within sixty (60) days after the effective date of this order, each respondent shall file with the Federal Trade Commission a written report setting forth in detail the manner and form of its compliance with this order.

IN THE MATTER OF

NORLIC IMPORT COMPANY, INC., ET AL.

MODIFYING ORDER, IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION AND WOOL PRODUCTS LABELING ACTS

Docket C-2583. Complaint, Oct. 22, 1974 — Modifying Order, Jan. 25, 1978.

This order modifying order to cease and desist issued October 22, 1974, 40 FR 6777, 84 F.T.C. 1173, substitutes for subparagraph 2 of the first "IT IS ORDERED" paragraph one that inserts the words "reprocessed or reused" before the first usage of the term "wool product."

ORDER MODIFYING ORDER TO CEASE AND DESIST

On March 28, 1977, respondents petitioned to reopen and modify the decision and order in this matter. Addenda to the petition were filed on April 7, 1977 and on May 25, 1977. The Bureau of Consumer Protection has filed an answer wherein it advises that it does not oppose respondents' request, as modified by respondents' filing of May 25, 1977.

The Commission has duly considered respondents' request and has determined that it should be granted.

It is ordered, That the proceeding be, and it hereby is, reopened;

It is further ordered, That the order to cease and desist be, and it hereby is, modified by striking subparagraph 2 of the first "IT IS FURTHER ORDERED" paragraph and substituting therefor the following:

> Importing or participating in the importation of reprocessed or reused wool products into the United States except upon filing bond with the Secretary of the Treasury in a sum double the value of said wool products and any duty thereon, conditioned upon compliance with the provisions of the Wool Products Labeling Act of 1939.

In the Matter of

LANCASTER COLONY CORPORATION, ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT AND SEC. 7 OF THE CLAYTON ACT

Docket 9101. Complaint, June 17, 1977 — Decision, Feb. 1, 1978

This consent order, among other things, requires a Columbus, Ohio manufacturer of machine-made glassware, and a Montvale, N.J. firm, similarly engaged, to present the Commission with evidence that their acquisition agreement has been terminated, and to return to each other all exchanged confidential documents. Further, during periods set forth in the order, these firms are required to provide the Commission with prescribed advance notice of any intention to acquire a machine-made glassware business, and refrain from consummating any such transaction, pending final Commission decision.

Appearances

For the Commission: *Peter E. Greene, Brian H. Siegel, Edward S. Atkinson, Jr., David J. Saylor* and *Alfred F. Dougherty.*

For the respondents: *Richard R. Murphey, Jr., Dunbar, Kiengle & Murphey,* Columbus, Ohio and *Ralph W. Brenner, Montgomery, McCracken, Walker & Rhoads,* Philadelphia, Pa. for Lancaster Colony Corp. *Edward Wolfe, White & Case,* New York City for Federal Paper Board Company Inc.

Complaint

The Federal Trade Commission, having reason to believe that the above-named respondents, each subject to the jurisdiction of the Commission, have entered into an acquisition agreement which, if consummated, would violate Section 7 of the Clayton Act, as amended, 15 U.S.C. 18, and Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45, that said agreement already constitutes a violation of the Federal Trade Commission Act, as amended, and that a proceeding in respect thereof would be in the public interest, hereby issues its complaint, pursuant to Section 11 of the Clayton Act, 15 U.S.C. 21, and Section 5(b), of the Federal Trade Commission Act, 15 U.S.C. 45(b), stating its charges as follows:

I

DEFINITION

1. For the purpose of this complaint, the following definition

shall apply: "Machine-made glassware" means all moderately priced soda-lime glass beverageware, tableware, food preparation glassware and novelty and ornamental glassware items produced by machine and employed in everyday use.

II

Federal Paper Board Company, Inc.

2. Federal Paper Board Company, Inc. (Federal Paper) is a corporation organized and existing under the laws of the State of New York, with a principal place of business at 75 Chestnut Ridge Road, Montvale, New Jersey.

3. Federal Paper through its unincorporated Federal Glass Company division (F.G.D.) produces machine-made glassware and sells said machine-made glassware throughout the United States.

4. In its fiscal year ended January 1, 1977, Federal Paper had net sales of approximately $393,580,000, and net income of approximately $22,589,000; F.G.D. had net sales of approximately $50,000,000 and income before allocation for taxes and corporate overhead of approximately $4,000,000.

5. F.G.D. is the third largest manufacturer of machine-made glassware in the United States.

6. F.G.D. is now and for many years has been a member of the American Glassware Association, which is a trade association made up of the major domestic manufacturers of machine-made glassware.

III

LANCASTER COLONY CORPORATION

7. Lancaster Colony Corporation (Lancaster Colony) is a corporation organized and existing under the laws of the State of Delaware, with a principal place of business at 37 West Broad St., Columbus, Ohio.

8. Lancaster Colony, through its subsidiary Indiana Glass Company, an Indiana corporation, produces machine-made glassware, and sells said machine-made glassware throughout the United States. Lancaster Colony also produces machine-made glassware through its subsidiary Lancaster Glass Corporation, and sells said machine-made glassware throughout the United States.

9. In its fiscal year ended June 30, 1976, Lancaster Colony had sales of approximately $174,500,000 and net income of approximately $8,236,000. Indiana Glass Company had sales of machine-made

glassware of approximately $36,488,445, and Lancaster Glass Company had sales of machine-made glassware of approximately $382,000.

10. Indiana Glass Company is the fifth largest manufacturer of machine-made glassware in the United States.

11. Indiana Glass Company is and for many years has been a member of the American Glassware Association, which is a trade association made up of the major domestic manufacturers of machine-made glassware.

IV

JURISDICTION

12. At all times relevant herein Federal Paper and Lancaster Colony have been engaged in the manufacture and sale of machine-made glassware in interstate commerce and are engaged in commerce as "commerce" is defined in Section 1 of the Clayton Act, as amended, 15 U.S.C. 12, and each is a corporation whose business is in or affecting commerce, as "commerce" is defined in Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. 44.

V

THE ACQUISITION AGREEMENT

13. On or about March 4, 1977 Federal Paper and Lancaster Colony agreed in principle to the acquisition by Lancaster Colony of all F.G.D. assets of Federal Paper. The proposed purchase agreement provides, *inter alia*, for the sale of the F.G.D. assets of Federal Paper in exchange for approximately $45,000,000.

VI

TRADE AND COMMERCE

14. Relevant lines of commerce are the manufacture and sale of machine-made glassware and submarkets thereof.

15. A relevant section of the country or geographic market is the entire United States.

16. The United States machine-made glassware market is highly concentrated with the combined market share of the four largest manufacturers estimated to be approximately 70 percent.

17. Barriers to entry into the manufacture of machine-made glassware and submarkets thereof are substantial.

VII

ACTUAL COMPETITION

18. Federal Paper and Lancaster Colony are and have been for many years actual competitors of each other in the manufacture and sale of machine-made glassware and submarkets thereof, and actual competitors of others engaged in the manufacture and sale of machine-made glassware and submarkets thereof throughout the United States.

VIII

EFFECTS

19. The effect of the proposed acquisition may be to substantially lessen competition or tend to create a monopoly in the relevant market in violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. 18, or Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45, in the following ways, among others:

(a) actual competition between Federal Paper and Lancaster Colony in the manufacture and sale of machine-made glassware and submarkets thereof will be eliminated;

(b) actual competition between competitors generally in the manufacture and sale of machine-made glassware and submarkets thereof may be lessened;

(c) Federal Paper will be eliminated as an actual substantial independent competitor in the manufacture and sale of machine-made glassware and submarkets thereof;

(d) concentration in the manufacture and sale of machine-made glassware and submarkets thereof will be increased and possibilities for eventual deconcentration may be diminished;

(e) mergers or acquisitions between other machine-made glassware manufacturers may be fostered, thus causing a further substantial lessening of competition and tendency toward monopoly in the relevant markets.

IX

VIOLATIONS CHARGED

20. The proposed acquisition by Lancaster Colony of the F.G.D. assets of Federal Paper (if consummated), the proposed Purchase Agreement between Lancaster Colony and Federal Paper (if executed), and the agreement in principle between Lancaster Colony and Federal Paper, constitute violations of Section 7 of the Clayton

Act, as amended, 15 U.S.C. 18, and are or would be unfair acts, practices or methods of competition in violation of Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45.

DECISION AND ORDER

The Commission having heretofore issued its complaint charging the respondents named in the caption hereof with violation of Section 5 of the Federal Trade Commission Act, as amended, and Section 7 of the Clayton Act, and the respondents having been served with a copy of that complaint, together with a notice of contemplated relief; and

The respondents, their attorneys, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Secretary of the Commission having thereafter withdrawn this matter from adjudication in accordance with Section 3.25(c) of its Rules; and

The Commission having considered the matter and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 3.25(f) of its Rules, the Commission hereby makes the following jurisdictional findings and enters the following order:

1. Respondent Lancaster Colony Corporation is a corporation, existing and doing business under and by virtue of the laws of the State of Delaware, with its office and principal place of business located in the City of Columbus, State of Ohio.

2. Respondent Federal Paper Board Company, Inc. is a corporation, existing and doing business under and by virtue of the laws of the State of New York, with its office and principal place of business located in the City of Montvale, State of New Jersey.

3. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

ORDER

Definition

For the purposes of this order the following definition shall apply: "Machine-made glassware" means all moderately priced soda-lime glass beverageware, tableware, food preparation glassware and novelty and ornamental glassware items produced by machine and employed in everyday use.

I

It is ordered, That Lancaster Colony Corporation (Lancaster Colony) and Federal Paper Board Company, Inc. (Federal Paper) do forthwith provide evidence that the agreement (acquisition agreement) whereby Lancaster Colony agreed to purchase all or substantially all of the assets of Federal Paper used by it in its business of the manufacture and sale of machine-made glassware which is conducted through its unincorporated Federal Glass Company Division has been terminated and each shall use its best efforts to forthwith return any confidential documents provided by either Lancaster Colony or Federal Paper to the other in connection with the acquisition agreement. Nothing herein contained shall relieve any party from any obligations of confidentiality imposed by agreement between them or by operation of law.

II

It is further ordered, That until December 31, 1980 neither Lancaster Colony nor Federal Paper shall acquire either directly or indirectly any part of the machine-made glassware business of the other, whether represented by securities or assets (other than products and securities acquired in the regular course of business) until sixty (60) days following receipt by the Director of the Bureau of Competition of the Federal Trade Commission of written notice of the proposed acquisition, which notice shall specifically refer to this order. If within sixty (60) days of receipt by the Director of said notice the Commission issues an administrative complaint challenging the proposed acquisition such proposed acquisition shall not be consummated nor shall any steps be taken to effectuate such proposed acquisition until the administrative complaint issued by the Commission is dismissed by the Commission, or until a final order as defined in 15 U.S.C. 21 and 45 is entered, or until a consent order is entered and served upon the respondents in that administrative proceeding. If within the aforesaid sixty (60) days the Bureau of

Competition receives any additional written position papers from either Lancaster Colony or Federal Paper and the Bureau recommends the issuance of a complaint, the Bureau shall promptly forward to the Commission such papers together with the written notice submitted to the Bureau Director. In the event that within sixty (60) days of the Director's receipt of the said notice the Commission issues an administrative complaint challenging the proposed acquisition the Bureau of Competition shall exert its best efforts to complete the administrative proceeding in an expedited manner.

III

It is further ordered, That until December 31, 1978 Lancaster Colony and Federal Paper each shall notify the Director of the Bureau of Competition of the Federal Trade Commission thirty (30) days prior to the consummation of any acquisition, merger, or sale of any of its machine-made glassware business, whether direct or indirect, (other than products and securities acquired or sold in the regular course of business) if (a) such transaction is with any company engaged in the business of manufacture and domestic sale of machine-made glassware; and (b) such company for the year preceding such transaction had total domestic sales of such machine-made glassware of $10,000,000 or more. Such notice shall contain all information requested by the Commission's pre-merger notification program (39 F.R. 35717-8, Oct. 3, 1974) on the forms as found in 1 CCH Trade Reg. Rep. ¶ 4540. If, during the period in which this paragraph is in effect the rules and notification report forms to implement Section 7A of the Clayton Act become effective, this paragraph shall from that date forward have no further effect.

IV

It is further ordered, That Lancaster Colony and Federal Paper each shall notify the Commission at least thirty (30) days prior to any proposed corporate change such as dissolution, assignment, or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change, which may affect compliance obligations arising out of this order.

V

It is further ordered, That Lancaster Colony and Federal Paper each shall, within sixty (60) days after service upon it of this order file with the Commission a written report setting forth in detail the manner and form in which it has complied with this order.

IN THE MATTER OF

AMERICAN CREDIT BUREAU, INC., ET AL.

Docket C-2608. Interlocutory Order, Feb. 3, 1978

Petition to vacate or modify consent order denied on grounds that respondents' allegations were insufficient because of public interest or changed conditions of law.

ORDER DENYING PETITION TO VACATE OR MODIFY CONSENT ORDER

Respondents, by petition filed pursuant to Rule 3.72(b)(2) on November 17, 1977, request that the Commission vacate or modify the consent order to cease and desist entered herein on December 4, 1974 (84 F.T.C. 1582), on the ground that changed conditions of law require such action.

The specific change of law underlying respondents' petition is the enactment of Pub. Law 95-109, the "Fair Debt Collection Practices Act," 15 U.S.C. 1601, *et seq.* (1977). The Act becomes effective on March 20, 1978.

Respondents allege that the Act regulates the same practices as are covered by the order, that the order differs substantially in terms from the Act, and that since the Act imposes severe penalties for violation, it would be in the public interest to vacate the order. Respondents further contend that certain sections of the Act are less restrictive than comparable sections of the order, that respondents would be competitively disadvantaged if they were subject to the order while their competitors were subject to the Act, and that, in the alternative, the order should be modified to bring it into conformity with the Act. The Director of the Bureau of Consumer Protection has filed an answer in opposition to respondents' petition.

The Commission, having carefully considered the petition and answer thereto, is of the opinion that (1) it would be premature and contrary to the public interest to grant respondents' request inasmuch as the Commission is currently conducting an investigation to determine whether or not respondents are in compliance with the cease and desist order, (2) the Fair Debt Collection Practices Act as a whole is more restrictive than the cease and desist order, and that those few instances in which the order may be more restrictive are necessary and proper as remedies fashioned by the Commission to redress abusive practices engaged in by respondents in violation of the Federal Trade Commission Act. There is nothing in the Fair Debt Collection Practices Act to prohibit the imposition of similar remedies in future cases brought under that Act if the circumstances so warrant, and (3) it would be premature to reopen the proceeding to modify or set aside the order since the Act has not yet taken effect.

Accordingly, the Commission having concluded that the allegations in respondents' petition are not sufficient to require that the order to cease and desist be modified or set aside because of the public interest or because of changed conditions of law:

It is ordered, That respondents' petition be, and it hereby is, denied.

IN THE MATTER OF

FORD MOTOR COMPANY

Docket 9001. Interlocutory Order, Feb. 10, 1978

On motion to withdraw matter from adjudication, Commission directed that pleadings of complaint counsel be furnished to the Commission, but not placed on the public record, to enable it to determine the probability that a settlement will be achieved.

ORDER

By his order of January 19, 1978, the Administrative Law Judge certified to the Commission an amended motion by respondent to withdraw this matter from adjudication for consideration of a consent order.

Beyond those facts, the posture of the motion becomes somewhat murky. Respondent's original motion recites that "complaint counsel do not oppose this motion," but this recital is absent from the amended motion.[1] Complaint counsel have not, however, executed the proposed consent order, for reasons which the Administrative Law Judge describes as including both some disagreement with its terms and the view that it would vary the terms of our earlier order (Dkt. C-2582) against the respondent, a variance complaint counsel presumably felt they could not agree to since "[a]ny modification of an outstanding order is exclusively within the jurisdiction and discretion of the Commission."[2]

Evidently the respective positions of respondent and complaint counsel with regard to the proposed consent order are fully set out in respondent's memorandum of December 23, 1977, complaint counsel's answer of January 16, 1978, and respondent's reply of January 18. These pleadings have not been sent forward to us, however, because of the Administrative Law Judge's opinion that "it would not be appropriate for the Commission to consider the substance of that memorandum [of December 23, 1977] before it withdraws the instant matter from adjudication."

The reasons for this are not elaborated, nor are they self-evident. Obviously, no *"ex parte"* problem exists, and if respondent in its memorandum concedes matters it had placed in issue the damage has already been done by submitting the memorandum to the initial trier of fact and law. Inasmuch as we are trying to determine, as the Administrative Law Judge did, the probability that a settlement will be achieved, respondent's memorandum and the additional pleadings could be of considerable assistance.

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[1] In his certification, however, the Administrative Law Judge characterizes the motion as "unopposed."

[2] While this statement is correct, its application in this context seems to reflect a misunderstanding of the significance of executing a proposed consent order. Complaint counsel's signature would indicate a recommendation that the Commission accept the order. Actual modification of the outstanding order would occur only if the Commission followed that recommendation. We make this observation only to obviate confusion in the future, since it appears here that complaint counsel could not unreservedly make such a recommendation.

Accordingly, it is ordered, That the pleadings of December 23, 1977, and January 16 and 18, 1978, be expeditiously transmitted to the Commission. They should not, however, be placed on the public record at this time.

IN THE MATTER OF

AIRCO, INC.

Docket 9098. Interlocutory Order, Feb. 15, 1978

Order establishing a protective order providing ten (10) days' notice before release of certain documents to be supplied in response to subpoena duces tecum.

ORDER

The Administrative Law Judge has certified to the Commission a paragraph undertaking to provide ten days' notice before release of certain documents to be supplied by Airco, Inc. in response to a subpoena *duces tecum*. If we so authorize, it is the Administrative Law Judge's intention to incorporate this paragraph in a protective order which he will grant to Airco. As our Rules now stand, a "ten-day notice" undertaking can only be made by the Commission itself.

The action requested by the Administrative Law Judge's certification is similar to that which the Commission took by order dated January 31, 1977, in *Exxon Corporation, et al.* The Commission has determined to authorize incorporation of paragraph 6 in the proposed protective order. The language set out in the Administrative Law Judge's certification will be modified, however, by deletion of the words "designated by Airco as confidential" and substitution therefor of the words "covered by this protective order." The coverage of such an order is of course for the Administrative Law Judge, not respondent, to determine.

So ordered.

IN THE MATTER OF

SECURITY PACIFIC MORTGAGE CORPORATION, AS SUCCESSOR TO KASSLER & CO.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION AND TRUTH IN LENDING ACTS

Docket C-2917. Complaint, Feb. 17, 1978 — Decision, Feb. 17, 1978

This consent order, among other things, requires a Denver, Colo. finance company to cease failing to provide consumers, in connection with the extension of credit, such material and disclosures as are required by Federal Reserve System regulations. Further, the company is required to make prescribed efforts to obtain information pertaining to third-party fees.

Appearances

For the Commission: *James T. Rohrer.*

For the respondent: *Gordon Greiner* and *Donald G. Palmer, Holland & Hart,* Denver, Colo.

COMPLAINT

Pursuant to the provisions of the Truth in Lending Act and the implementing regulation promulgated thereunder, and the Federal Trade Commission Act, and by virtue of the authority vested in it by said Acts, the Federal Trade Commission having reason to believe that Security Pacific Mortgage Corporation, as successor in interest to Kassler & Co., a corporation, hereinafter referred to as respondent, has violated the provisions of said Acts and implementing regulation, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent Kassler & Co. was a corporation organized, existing and doing business under and by virtue of the laws of the State of Colorado, with its principal office and place of business located at Diamond Hill Office Park, 2460 West 26th Ave., Denver, Colorado.

PAR. 2. Security Pacific Mortgage Corporation is a "successor and assign" of Kassler & Co., having merged with Kassler in 1974, after the acts and practices alleged in the complaint. Security Pacific Mortgage Corporation is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its office and principal place of business located at 2460 West 26th Ave., Denver, Colorado.

PAR. 3. Respondent is now and for some time last past has been engaged in the business of arranging for and providing to the public, for a fee, mortgage loans secured by real property.

PAR. 4. In the ordinary course and conduct of its business as aforesaid, respondent regularly arranges for the extension of consumer credit, as "arrange for extension of credit" and "consumer credit" are defined in Section 226.2 of Regulation Z, the implementing regulation of the Truth in Lending Act, duly promulgated by the Board of Governors of the Federal Reserve Board.

PAR. 5. Subsequent to July 1, 1969, respondent, in connection with its arrangement for the extension of consumer credit, has provided customers with required cost disclosure statements which:

A. Fail to include in the finance charge a charge imposed directly or indirectly by the creditor payable directly or indirectly by the customer to a third party, such charge being incident to the extension of credit, as required by Section 226.4(a) of Regulation Z, when such charges were within the actual or constructive knowledge of the respondent and within the purview of its relationship with the customer as required by Section 226.6(d) of Regulation Z.

B. Fail to state the finance charge accurately as required by Section 226.8(d)(3) of Regulation Z.

C. Fail to disclose, in accordance with Section 226.8(d)(2) of Regulation Z, any finance charge paid directly or indirectly with the creditor's knowledge to another person as required by Section 226.8(e)(1).

D. Fail to state accurately the amount of credit by failing to exclude from such amount financed the items set forth in Section 226.8(e)(1) of Regulation Z as required by Section 226.8(d)(1) of Regulation Z.

E. Fail to disclose the annual percentage rate computed in accordance with the requirements of Section 226.5 of Regulation Z accurately to the nearest quarter of one percent, as required by Section 226.8(b)(2) of Regulation Z.

PAR. 6. Subsequent to July 1, 1969, in the ordinary course and conduct of its business as aforesaid, respondent arranged for the extension of credit in transactions in which a security interest is acquired in real property which is used as a principal residence of the customer. The customers thereby have the right to rescind the transaction, as provided by Section 226.9 of Regulation Z. As set out in Paragraph Five herein, respondent has failed and continues to fail to deliver to some of its customers the material disclosures required by Regulation Z. Therefore, some of the respondent's customers have not been afforded the three (3) day right of rescission from the date of consummation of the transaction or date of delivery of material disclosures, whichever is later, as set out in Section 226.9(a) of Regulation Z. Respondent has not given notice of this right to rescind as required by Section 226.9(b) of Regulation Z, in the manner and form specified therein.

PAR. 7. Pursuant to Section 103(q) of the Truth in Lending Act, respondent's aforesaid failures to comply with the requirements of Regulation Z constitute a violation of that Act and, pursuant to Section 108(c) thereof, respondent thereby violated the Federal Trade Commission Act.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Atlanta Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act, as amended; and

The respondent and its attorney and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter pursuant to Section 2.34 of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Proposed respondent Kassler & Co. was, at the time of the acts alleged in the Commission's complaint, a corporation organized, existing and doing business under and by virtue of the laws of the State of Colorado, with its office and principal place of business located at Diamond Hill Office Park, 2460 West 26th Ave., Denver, Colorado.

2. Security Pacific Mortgage Corporation is a successor and assign of Kassler & Co., having merged with Kassler in 1974, after the acts and practices alleged in the complaint. Security Pacific Mortgage Corporation is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its office and principal place of business located at 2460 West 26th Ave., Denver, Colorado. Security Pacific Mortgage Corporation is thus bound by this order.

3. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

It is ordered, That respondent Security Pacific Mortgage Corporation, as successor in interest to Kassler & Co., a corporation, its successors and assigns, and its officers, and respondent's agents, representatives and employees, directly or through any corporation, subsidiary, division or other device, in connection with the extension of "consumer credit" or arranging for "consumer credit", as defined in Regulation Z (12 C.F.R. 226) of the Truth in Lending Act [15 U.S.C. 1601-65 (1970), as amended, 15 U.S.C. 1601-65(a), (Supp. IV, 1974)], do forthwith cease and desist from:

1. Failing to include in the stated finance charge, as required by Section 226.4(a) of Regulation Z, any monies payable directly or indirectly by the customer to any third party who may have referred consumer loans to them or who may have assisted them in arranging for consumer credit, of which respondent is aware or should be aware through its reasonable effort.

2. Failing to disclose the amount of the finance charge accurately, as required by Section 226.8(d)(3) of Regulation Z.

3. Failing to disclose the amount of any "prepaid finance charge," as directed in Section 226.8(d)(2) of Regulation Z.

4. Failing to state accurately the amount of credit by failing to exclude from such amount the items set forth in Section 226.8(e)(1) of Regulation Z, as required by Section 226.8(d)(1) of Regulation Z.

5. Failing to disclose the annual percentage rate accurately to the nearest quarter of one percent, in accordance with Section 226.5 of Regulation Z, as required by Section 226.8(b)(2) of Regulation Z.

6. Failing to make reasonable efforts to obtain or to estimate information required for disclosures as is allowed by Section 226.6(f) of Regulation Z, and thus failing to accurately disclose the finance charge, as required by Section 226.8(d)(3) of Regulation Z.

7. Failing in any consumer credit transaction or advertising to

make all disclosures determined in accordance with Sections 226.4 and 226.5 of Regulation Z at the time and in the manner, form and amount required by Sections 226.6, 226.8 and 226.10 of Regulation Z.

It is further ordered, That the respondent henceforth obtain from each person receiving consumer credit from it a completed and signed statement relating to monies or obligations to pay monies which are payable, directly or indirectly, by the customer to any third party who may have referred the customer to respondent or who may have assisted the customer in arranging for consumer credit with respondent. A sample of such a form is attached hereto as Appendix A. In each instance in which respondent has obtained such a completed form and in which a customer has indicated thereon that he is not liable for and has not paid a fee to any other person in connection with the loan, respondent shall be deemed to have made sufficient reasonable efforts as required by subparagraph 1 of this order, unless respondent otherwise has actual knowledge of monies or fees payable by the customer to any third party.

It is further ordered, That respondent shall, within sixty (60) days after service of this order upon respondent, file with the Commission a report showing the manner and form in which it has complied and is complying with each and every specific provision of this order.

It is further ordered, That the respondent corporation shall forthwith distribute a copy of this order to each of its operating divisions.

It is further ordered, That respondent notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance obligations arising out of the order.

APPENDIX A

Customer Statement of Third Party Fees

1. Have you paid or are you liable for the payment of a fee to any person who has assisted you with or who has arranged for your application to Security Pacific Mortgage Corporation for this loan?

Yes

No

2. If your answer above was "Yes," please state the amount of the fee paid or to be paid to such person.

$ _____

3. If your answer to question 1 was "Yes," please state the name and address of such person.

Name ________________

Address ____________________

____

I have read and understand this document, and affirm that the answers given are true to the best of my knowledge.

Date ***Customer***

Customer

IN THE MATTER OF

FRUEHAUF CORPORATION, INC.

ORDER, OPINION, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT AND SECTION 7 OF THE CLAYTON ACT

Docket 8972. Complaint, June 21, 1974 — Final Order, Feb. 22, 1978

This order, among other things, requires a Detroit, Mich. truck trailer manufacturer to divest itself, within one year from the date of the order, of Kelsey-Hayes, a Romulus, Mich. manufacturer of automotive components, excluding those operations unique to Kelsey-Hayes' Aerospace Group and R-V Agriculture Group; and to refrain, for a ten-year period, from acquiring any concern engaged in manufacturing, distributing, or selling heavy duty wheels, antiskid braking devices, or truck trailers.

Appearances

For the Commission: *K. Keith Thurman, George J. Wright, Richard L. Williams* and *Tom D. Smith.*

For the respondent: *John R. Ferguson, William H. Wentz, Phillip A. Proger, Janine H. Coward, Alan S. Ward* and *Warren Daane, Baker, Hostetler, Frost & Towers,* Washington, D.C.

COMPLAINT

The Federal Trade Commission having reason to believe that Fruehauf Corporation, a corporation subject to the jurisdiction of the Commission, has acquired the stock of Kelsey-Hayes Company, a corporation, in violation of Section 7 of the Clayton Act, as amended, (15 U.S.C. 18), and Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45(a)(1)), and that a proceeding in respect thereof would be in the public interest, hereby issues this complaint, pursuant to Section 11 of the Clayton Act (15 U.S.C. 21) and Section 5 of the Federal Trade Commission Act (15 U.S.C. 45(a)(6)(b), stating its charges in that respect as follows:

I. DEFINITIONS

1. For the purpose of this complaint, the following definitions shall apply:

(a) "Wheels" include wheels, rims, hubs and brake drums.

(b) "Heavy duty" refers to components for application on on-highway vehicles such as trucks, truck tractors, buses, truck trailers and container chassis having a gross vehicle weight (GVW) of 14,000 lbs. or more.

(c) "Antiskid braking device" is three matched components consisting of a sensor, a computer and a valve designed to control braking during a potential skid situation. [2]

(d) "Truck Trailers" are all types of truck trailers (product class code 37150) reported by the U.S. Bureau of Census in its current industrial report of shipments of truck trailers for 1972.

(e) "Market" includes all shipments of the relevant products manufactured in the United States or imported into the United States.

II. FRUEHAUF CORPORATION

2. Respondent, Fruehauf Corporation (hereinafter "Fruehauf"), is now, and was at the time of the acquisition hereinafter set forth, a Michigan corporation with its principal office and place of business located at 10900 Harper Ave., Detroit, Michigan.

3. In 1972, Fruehauf had sales and rentals of $550.4 million and assets of $556.6 million. In that year it was the 245th largest publicly held industrial corporation in the nation in total sales and revenues and ranked 207th in assets.

4. Fruehauf, prior to and following the acquisition hereinafter set forth, was and is the nation's largest and most vertically integrated truck trailer manufacturer. Fruehauf presently produces truck trailers in twelve manufacturing locations in the United States. Ninety-six domestic branch operations owned by Fruehauf sell and service truck trailers in the United States and they constitute the most extensive service and distribution system in the nation's truck trailer industry. Fruehauf produces, sells and services several different types of truck trailers including all types of van trailers, platform, tank, bulk commodity and dry material, pole and logging, dump, low-bed heavy haulers, van size containers and container chassis.

5. At all times relevant herein, Fruehauf sold and shipped its products throughout the United States and was engaged and is now engaged in commerce as "commerce" is defined in the Clayton Act and in the Federal Trade Commission Act.

III. KELSEY-HAYES COMPANY

6. Prior to its acquisition by Fruehauf as hereinafter set forth, Kelsey-Hayes Company (hereinafter "Kelsey-Hayes"), was a Delaware corporation with its principal office and place of business located at 38481 Huron River Drive, Romulus, Michigan. [3]

7. In the fiscal year ending August 31, 1973, Kelsey-Hayes had

sales of $453.7 million and assets of $243.0 million. In 1972, Kelsey-Hayes was the 281st largest publicly held industrial corporation in the nation in total sales and revenues and ranked 363rd in assets.

8. In 1972, approximately 72 percent of Kelsey-Hayes' sales were of products and components for automobiles, trucks, and truck trailers.

9. In 1972, Kelsey-Hayes was the nation's largest manufacturer of wheels for use in the manufacture of automobiles. Kelsey-Hayes was and is a significant supplier of heavy duty wheels including truck trailer wheels. In 1972, Kelsey-Hayes was a key supplier of heavy duty truck wheels to both original equipment manufacturers and replacement parts distributors and the major independent supplier of both drum brake assemblies and brake drums to the automotive industry. Kelsey-Hayes has developed and plans to manufacture and sell a heavy duty antiskid braking device of the type which will be standard equipment on all heavy duty trucks, truck tractors and truck trailers manufactured in the United States beginning September 1, 1974.

10. At all times relevant herein, Kelsey-Hayes sold and shipped its products throughout the United States and was engaged and is now engaged in commerce as "commerce" is defined in the Clayton Act and in the Federal Trade Commission Act.

IV. THE ACQUISITION

11. On or about October 31, 1973, Fruehauf Manufacturing Company (hereinafter "Fruehauf Manufacturing"), an inactive wholly-owned subsidiary of Fruehauf, was merged into Kelsey-Hayes, whereby Kelsey-Hayes survived as a wholly-owned subsidiary of Fruehauf. To consummate the merger, Fruehauf issued approximately 3,804,915 shares of Fruehauf common stock at an approximate value of $99 million to Fruehauf Manufacturing and all Kelsey-Hayes common stock was then converted into Fruehauf common stock owned by Fruehauf Manufacturing in the ratio of five shares of Fruehauf common stock for four shares of Kelsey-Hayes common stock. Kelsey-Hayes has been operated as a Fruehauf subsidiary since the acquisition.

V. TRADE AND COMMERCE

12. The relevant geographic market is the United States as a whole. The relevant product markets are: [4]

(a) Manufacture and sale of heavy duty wheels;

(b) Manufacture and sale of truck trailer wheels;

(c) Manufacture and sale of cast spoke truck trailer wheels, exclusive of rims;

(d) Manufacture and sale of heavy duty antiskid braking devices; and

(e) Manufacture and sale of truck trailers.

A. HEAVY DUTY WHEELS

13. The market for heavy duty wheels was $263.6 million in 1972. Shipments in the truck trailer wheel market were $72.7 million in that year. In 1972, shipments of cast spoke truck trailer wheels, exclusive of rims, were $35.0 million.

14. Concentration in the manufacture and sale of heavy duty wheels is high with the top four firms accounting for 69 percent, and the top eight firms accounting for 94 percent of the market in 1972. Concentration is similarly high in the manufacture and sale of truck trailer wheels with the top four firms accounting for 63 percent, and the top eight firms accounting for 87 percent of the market in 1972. Concentration in the manufacture and sale of cast spoke truck trailer wheels, exclusive of rims, is very high, with the top four firms accounting for 91 percent, and the top eight firms accounting for 100 percent of the market in 1972.

a. *Vertical Relationships*

15. Entry into the manufacture and sale of heavy duty wheels is difficult. The manufacture and sale of such wheels requires large financial resources, sophisticated technological skills required of a foundry and an effective distribution system. Few firms possess such prerequisites for entry. [5]

16. In 1972, Kelsey-Hayes was the second largest domestic producer of heavy duty wheels, the eighth largest domestic producer of truck trailer wheels, and the fourth largest domestic producer of cast spoke truck trailer wheels, exclusive of rims. In 1972, Kelsey-Hayes' share of the market for heavy duty wheels was 15 percent, its share of the market for truck trailer wheels was 3.7 percent, and its share of the market for cast spoke truck trailer wheels, exclusive of rims, was 7.8 percent.

17. In 1972, Fruehauf accounted for 4.8 percent of all heavy duty wheel purchases. Fruehauf was the largest purchaser of truck trailer wheels and cast spoke truck trailer wheels, exclusive of rims, in that year, accounting, respectively, for 17.9 percent and 17.5 percent of such purchases. Fruehauf purchased 7 percent of its requirements

for truck trailer wheels in 1972 from Kelsey-Hayes and 93 percent from all other suppliers.

18. With the availability of Fruehauf's branches as outlets for selling and servicing of Kelsey-Hayes heavy duty wheels and the aid of the Fruehauf domestic sales force, Kelsey-Hayes' position in the heavy duty wheel market will be strengthened.

b. *Potential Competition*

19. Fruehauf was one of the few most likely competitors of Kelsey-Hayes in the heavy duty wheel market prior to the acquisition. Fruehauf had conducted several studies relating to fabricating its own truck trailer wheels and had done extensive development work with truck trailer wheel manufacturers prior to the acquisition of Kelsey-Hayes. Fruehauf, prior to the acquisition of Kelsey-Hayes, had already integrated into the manufacture of axles and was the only truck trailer manufacturer which fabricated truck trailer axles. Such axles were not only for its own use but also were sold to other truck trailer manufacturers. Similarly, Fruehauf had integrated into aluminum extrusion, a major truck trailer component, and was the only truck trailer manufacturer which produced its own aluminum extrusions. Such extrusions not only were used by Fruehauf but also sold to other truck trailer manufacturers. [6]

20. By virtue of its position as the most vertically integrated truck trailer manufacturer in the United States, its production of truck trailer axles and possession of attendant technological skill, its marketing ability, its financial resources and its demonstrated interest in entering the heavy duty wheel market, Fruehauf was, prior to October 31, 1973, one of the few most likely entrants into the manufacture and sale of heavy duty wheels.

B. HEAVY DUTY ANTISKID BRAKING DEVICES

21. Performance standards set forth in Department of Transportation Federal Motor Vehicle Safety Standard 121[1] will require heavy duty antiskid braking devices on all heavy duty trucks, truck tractors and truck trailers manufactured in the United States after September 1, 1974.

22. Entry into the manufacture and sale of heavy duty antiskid braking devices is difficult. The development, manufacture, and sale of heavy duty antiskid braking devices require large financial resources, sophisticated technological skill and an effective distribu-

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[1] 49 C.F.R. 571.121.

tion and service system. Few firms possess such prerequisites for entry.

23. In the year following September 1, 1974, domestic sales of heavy duty antiskid braking devices will be approximately $80 million. Heavy duty antiskid braking devices having application on truck trailers will comprise approximately 30 percent of the heavy duty antiskid braking device market in the year following September 1, 1974.

24. Concentration in the heavy duty antiskid braking device will be high. Fewer than ten firms will be able to manufacture production quantities of heavy duty antiskid braking devices by September 1, 1974.

25. Kelsey-Hayes is a leading producer and developer of heavy duty antiskid braking devices as well as a leading manufacturer of automobile antiskid braking devices.

26. Kelsey-Hayes' share of the heavy duty antiskid braking device market is projected to be approximately 30 percent in the year following September 1, 1974.

27. Purchases of heavy duty antiskid braking devices by Fruehauf will comprise approximately 8 percent of total heavy duty antiskid braking device purchases in the year following September 1, 1974. [7]

28. With the availability of Fruehauf's branches as outlets for selling and servicing of Kelsey-Hayes heavy duty antiskid braking devices and the aid of the Fruehauf domestic sales force, Kelsey-Hayes' position in the heavy duty antiskid braking device market will be strengthened.

C. TRUCK TRAILERS

29. In 1972, the total value of truck trailer shipments in the United States was $886.2 million.

30. The truck trailer market is highly concentrated. In 1972, the top four firms accounted for 55.0 percent of total truck trailer shipments and the top eight firms accounted for 69.3 percent.

31. In 1972, Fruehauf's share of the truck trailer market was approximately 25 percent.

32. Entry into the manufacture and sale of truck trailers to significant users is difficult. A successful manufacturer and seller of truck trailers must possess ample financial resources, have manufacturing, assembling and marketing skill and have access to reliable sources of supply for component parts.

33. The prompt supply of truck trailer components is of major importance to truck trailer manufacturers due to short delivery

deadlines often set by truck trailer purchasers. Through the acquisition of Kelsey-Hayes, Fruehauf has captured a secure source of supply for truck trailer wheels as well as a source of heavy duty antiskid braking devices. This secure source of supply to Fruehauf of truck trailer wheels and heavy duty antiskid braking devices gives Fruehauf a significant advantage over its competitors, particularly in periods of scarce supply of either of these truck trailer components.

34. The advantage gained by Fruehauf over its competitors through its acquisition of a secure source of supply for component parts produced by Kelsey-Hayes is magnified by the probability that truck trailer customers who purchase truck trailers from Fruehauf during periods of components' scarcity will continue to purchase truck trailers from Fruehauf in the future. Truck trailer customers generally receive better trade-in terms for Fruehauf trailers at Fruehauf branches than they do from other manufacturers, giving these customers an incentive to continue purchasing from Fruehauf. Many truck trailer customers are trucking fleet operators who seek standardization in their fleets to minimize parts stocking problems and simplify maintenance and therefore are likely to continue [8] purchasing truck trailers from their present source. Fruehauf utilizes many component parts peculiar to Fruehauf trailers when the truck trailers are manufactured. Thus, double stocking of the same type of parts is necessary when a trucker mixes other makes of truck trailers with Fruehauf trailers in his fleet.

VI. EFFECTS OF THE ACQUISITION

35. The effects of the acquisition of Kelsey-Hayes by Fruehauf may be substantially to lessen competition or tend to create a monopoly in the manufacture and sale of heavy duty wheels, truck trailer wheels, cast spoke truck trailer wheels, exclusive of rims, heavy duty antiskid braking devices and truck trailers throughout the United States in violation of Section 7 of the Clayton Act, as amended, and the effects of the acquisition may be to unreasonably restrain trade and hinder competition unduly in the manufacture and sale of heavy duty wheels, truck trailer wheels, cast spoke truck trailer wheels, exclusive of rims, heavy duty antiskid braking devices and truck trailers, thereby constituting a restraint of trade and an unfair act and practice in commerce, in violation of Section 5 of the Federal Trade Commission Act, as amended, in the following ways among others:

(a) actual and potential producers of heavy duty wheels other than

Kelsey-Hayes have been and may be foreclosed from selling to a substantial purchaser of heavy duty wheels.

(b) Kelsey-Hayes' position in the heavy duty wheel market will be strengthened.

(c) Actual and potential producers of truck trailer wheels other than Kelsey-Hayes have been and may be foreclosed from selling to the leading purchaser of truck trailer wheels. [9]

(d) Kelsey-Hayes' position in the truck trailer wheel market will be strengthened.

(e) actual and potential producers of cast spoke truck trailer wheels, exclusive of rims, other than Kelsey-Hayes have been and may be foreclosed from selling to the leading purchaser of such wheels.

(f) Kelsey-Hayes' position in the market for cast spoke truck trailer wheels, exclusive of rims, will be strengthened.

(g) Substantial potential competition between Fruehauf and manufacturers of heavy duty wheels, including Kelsey-Hayes, has been eliminated.

(h) Potential competition in the heavy duty wheel market has been substantially lessened.

(i) Sales by Kelsey-Hayes of heavy duty antiskid braking devices may be increased through, and competitive suppliers of such products foreclosed from, the actual and potential purchases of Fruehauf.

(j) Kelsey-Hayes' position in the heavy duty antiskid braking device market will be strengthened at the expense of Kelsey-Hayes' actual and potential competitors.

(k) Truck trailer manufacturers who are competitors of Fruehauf have been or may be foreclosed from a source of supply for heavy duty wheels and heavy duty antiskid braking devices.

(l) Barriers to entry in each of the relevant markets have been raised.

(m) The dominant position of Fruehauf in the truck trailer market will be strengthened. [10]

VII. VIOLATIONS CHARGED

36. The acquisition of Kelsey-Hayes by Fruehauf constitutes a violation of Section 7 of the Clayton Act, as amended, (15 U.S.C. 18), and constitutes a violation of Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45).

INITIAL DECISION BY THOMAS F. HOWDER, ADMINISTRATIVE LAW JUDGE

JULY 31, 1977

PRELIMINARY STATEMENT

This case concerns the effect on competition arising from the merger joining the Fruehauf Corporation ("Fruehauf") and the Kelsey-Hayes Company ("Kelsey") on October 31, 1973. The [2] Federal Trade Commission on June 21, 1974 issued a complaint challenging the merger as violative of Section 7 of the Clayton Act, as amended, (15 U.S.C. 18) and Section 5 of the Federal Trade Commission Act (15 U.S.C. 45).*

The Commission's complaint alleges that competition will be lessened in each of three basic markets, *viz.*, truck trailers, heavy duty antiskid braking devices, and heavy duty wheels — and also in two submarkets, truck trailer wheels (later abandoned by complaint counsel) and cast spoke truck trailer wheels, exclusive of rims. The anticompetitive effects alleged were vertical foreclosure of competing companies from access to markets and/or sources of supply and entrenchment of the merged firms in their respective markets. The complaint also alleges that Fruehauf has been removed as a potential competitor of Kelsey in the manufacture and sale of heavy duty wheels.

On August 19, 1974, respondent Fruehauf filed an answer to the complaint admitting the merger and certain corporate and jurisdictional facts, but denying the substantive allegations thereof.

Prehearing conferences were held in Washington, D.C. on September 10, 1974 and February 4, 1975. Discovery was actively pursued by both parties. Proposed exhibit lists with copies of proposed exhibits and witness lists with narrative summaries of expected testimony were exchanged by the parties prior to trial. Both parties submitted trial briefs in support of their respective positions in this matter. [3]

All hearings in the case were held in Washington, D.C. Presentation of the case-in-chief began on October 20, 1975 and concluded on December 5, 1975. Presentation of Fruehauf's defense began on March 22, 1976 and continued through May 4, 1976. Complaint counsel began its rebuttal case with hearings on June 1, 2 and 11, 1976. A rebuttal subpoena was issued to Fruehauf on May 20, 1976 with the return on September 13, 1976. Rebuttal hearings resumed on October 12, 1976 and concluded on November 8, 1976. Fruehauf presented its surrebuttal with hearings on November 29, 1976, December 1 and 2, 1976 and February 10, 1977.

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* Complaint counsel's "Reply to Respondent's Motion for More Definite Statement" (dated July 29, 1974) indicated that the only theories of liability which they would assert were those encompassed by Section 7 of the Clayton Act.

The record (which includes a transcript of 7678 pages and 502 exhibits) was closed on March 29, 1977, following the resolution of various matters regarding exhibits, transcript corrections and *in camera* materials. Proposed findings were filed by the parties on May 9, 1977 and reply findings on June 7, 1977.

Any motions not heretofore or herein specifically ruled upon, either directly or by the necessary effect of the conclusions in this Initial Decision, are hereby denied.

This proceeding is before me upon the complaint, answer, testimony and other evidence, proposed findings of fact and conclusions of law filed by counsel supporting the complaint and by counsel for respondent. The proposed findings of fact, conclusions and arguments of the parties have been carefully considered, and those findings not adopted either in the form proposed or in substance are rejected as not supported by the evidence or as involving immaterial issues not necessary for this decision.

Certain abbreviations, including the following are used in this decision:

CX - Commission's Exhibits.

RX - Respondent's Exhibits. [4]

CC's 1st RAF - Complaint Counsel's Initial Request for Admission of Facts.

CC's 1st RACF - Complaint Counsel's Initial Request for Admission of Confidential Facts.

R's 1st RAF - Respondent's Initial Request for Admission of Facts.

R's 1st RACF - Respondent's Initial Request for Admission of Confidential Facts.

The transcript of testimony is referred to with the last name of the witness and the page number or numbers upon which the testimony appears.

Having heard and observed the witnesses and after having carefully reviewed the entire record in this proceeding, together with the proposed findings and conclusions submitted by the parties, I make the following findings:

FINDINGS OF FACT

I. IDENTITY AND BUSINESS OF RESPONDENT

1. Respondent Fruehauf is a publicly held corporation organized

and existing under the laws of the State of Michigan, with its principal office and place of business at 10900 Harper Ave., Detroit, Michigan. (Complaint and Answer, Para. 2.)

2. In 1972, Fruehauf had sales and rentals of $550.4 million and assets of $556.6 million. According to Fortune magazine, Fruehauf in 1972 was the nation's 245th largest publicly held industrial corporation in total sales and revenues and the 207th largest in total assets. (Complaint and Answer, Para. 3; CX 544A.) [5]

3. Fruehauf manufactures numerous types of truck trailers including van, platform, tank, bulk commodity and dry materials, pole and logging, dump, low-bed heavy haulers, van size containers, and container chassis. Fruehauf has established ninety-seven branches to provide sales, maintenance and service throughout the nation. (Complaint and Answer, Para. 4.) Both before and following the acquisition, Fruehauf has been the nation's largest truck trailer manufacturer. (CX 544A.)

4. At all times relevant herein, Fruehauf sold and shipped its products throughout the United States and was engaged in commerce as "commerce" is defined in the Clayton Act and in the Federal Trade Commission Act. (Complaint and Answer, Para. 5.)

II. THE ACQUISITION

5. On October 31, 1973 Fruehauf issued approximately 3,804,915 shares of Fruehauf common stock at an approximate value of $99 million to Fruehauf Manufacturing Company, an inactive wholly-owned subsidiary of Fruehauf. Fruehauf Manufacturing Company then exchanged these shares of Fruehauf common stock for all the common stock of Kelsey-Hayes in the ratio of five shares of Fruehauf common stock for four shares of Kelsey-Hayes common stock. Fruehauf Manufacturing was thereby merged into Kelsey-Hayes and Kelsey-Hayes survived as a wholly-owned subsidiary of Fruehauf. Kelsey-Hayes has been operated as a Fruehauf subsidiary since the acquisition. (Complaint and Answer, Para. 11.) [6]

III. THE ACQUIRED COMPANY

6. Prior to October 31, 1973 Kelsey-Hayes was a Delaware corporation with its principal office and place of business at 38381 Huron River Drive, Romulus, Michigan. (Complaint and Answer, Para. 6.)

7. For the fiscal year ending August 31, 1972 Kelsey-Hayes had net sales of $454.7 million and assets of $243.0 million. According to Fortune magazine, Kelsey-Hayes in 1972 was the 281st largest

publicly held industrial corporation in the United States in total net sales and the 363rd largest in total assets. (Complaint and Answer, Para. 7; CX 544A.)

8. Kelsey-Hayes manufactures various component parts for the automotive industry, such as automobile wheels, brake drums and drum brake assemblies. It also manufactures heavy duty wheels for use on trucks and truck trailers. In addition, Kelsey-Hayes in 1975 was the leading supplier of heavy duty antiskid braking devices to heavy duty truck, truck tractor and truck trailer manufacturers. (Complaint and Answer, Para. 9; see proposed finding 46 of complaint counsel *in camera*.)

9. At all times relevant herein, Kelsey-Hayes sold and shipped its products throughout the United States and was engaged in commerce as "commerce" is defined in the Clayton Act and in the Federal Trade Commission Act. (Complaint and Answer, Para. 9, 10.)

IV. THE GEOGRAPHIC MARKET

10. There is no dispute and it is found that the relevant geographic market is the United States as a whole. (CX 544B.) [7]

V. HEAVY DUTY ANTISKID BRAKING DEVICE MARKET

11. The term "antiskid braking device" refers to certain safety equipment installed on the braking systems of an air-braked vehicle. This mechanism is designed to monitor and, if necessary, to override the driver's action during braking to prevent wheel lock-up and a possible skid. The device consists principally of three matched components: (1) a sensor which determines the speed at which a wheel is rotating; (2) a computer or logic module which calculates the speed at which the wheel should rotate in order to achieve maximum braking efficiency; and (3) a valve which regulates the air pressure so as to release the brakes momentarily in the event of an impending skid. (Campanini 379-80, 402, 407-09; Lindquist 531-32; Perry 662-63; Deibel 1012; DeClaire 1068-69; Denholm 1667; Henry 2438-39; Bell 2601, 2672-73; Robins 2903; Megginson 4198-99.)

12. In the main, development of the antiskid braking device was a direct result of Federal Motor Vehicle Safety Standard (FMVSS) 121 (49 C.F.R. 571.121 as amended), promulgated by the National Highway Traffic Safety Administration ("NHTSA") of the U.S. Department of Transportation. FMVSS 121 is a performance standard regulating stopping distances for heavy duty vehicles. Although this regulation does not specify the use of an antiskid braking device, the device is the only product presently available

which satisfies the standard. (Campanini 450; Perry 664; Deibel 1043.)

13. In promulgating FMVSS 121, the Department of Transportation set braking performance standards which had to be met on the majority of heavy duty air-braked truck trailers manufactured after January 1, 1975, and air-braked trucks and truck tractors manfactured after March 1, 1975. (CX 195; 550C; 555C; Campanini 408, 413, 450; Perry 664; Deibel 1005; Heller 4150-51; Polkow 4323.) [8]

14. Initially one antiskid device was required for each braked axle of an air-braked vehicle. However, a January 1976 modification of FMVSS 121 lengthened the required stopping distances and allowed heavy duty trucks and truck tractors to meet the standard without the necessity for an antiskid device on the front axle of those vehicles. The number of systems required on a truck trailer remains one per axle. (Heller 4184-85; tr. 4354-56 *in camera.*)

15. An antiskid braking device is a distinct product which is necessary, per government regulation, for the manufacture of a truck trailer; a product for which there presently is no substitute. For reasons set forth herein, I find that the antiskid braking device market is an economically meaningful market within which to analyze the competitive effects of the merger in issue.

A. *Market Structure*

16. Concentration in the manufacture and sale of antiskid devices is high. According to the record, only the following seven companies actively competed in the market in 1975 and 1976: Kelsey-Hayes, the leading seller, Eaton Corporation, Wagner Electric Company, B.F. Goodrich, A.C. (division of General Motors), Rockwell International, and Berg/Fiat. (Campanini 420; Perry 677; Deibel 1020; tr. 1129 *in camera;* Denholm 1672-73; Vause 2211; Henry 2439, 2455; tr. 2608-09 *in camera;* Robins 2903). The top two firms accounted for over 50 percent of the total 1975 unit sales of antiskid devices and the top four accounted for 74 percent. (Nelson 6531 *in camera.*)

17. Antiskid devices are sold in the United States to truck tractor and truck trailer manufacturers, original equipment manufacturers ("OEM"), who install the device on the axles of the vehicles. [9]

18. The major suppliers of antiskid devices each developed or obtained their own designs for their respective antiskid systems. They either manufacture one or more of the three major components themselves, or supervise their manufacture by subcontractors. (CX 190D, CX 191P-Q, CX 585B; Campanini 422-23; tr. 683 *in camera;*

Deibel 1021–22; DeClaire 1071–72, 1075–76; Vause 2211; Megginson 4215, 4224, 4226, 4239; Schimpf 4305.)

19. The antiskid device has initially been marketed as a "system," the three major components being assembled by the seller and sold as a "package" or "kit" to the OEM. (Bachman 63; Allen 187; Stein 345). Some question was raised in the record as to whether the device will continue to be sold as a system or whether the three major components can be or will be sold separately to the OEM.

20. Antiskid can only exist as a components market to the extent that the separate components can be interchanged and assembled by the OEM's for installation on their vehicles. Standardization of the three major components would permit such an interchange; that is, although one supplier's component may not be physically identical to that of another, common performance characteristics would permit compatibility among the various sensors, valves, and logics. (Nelson 7181; Heller 4161; Campanini 509.)

21. At present, most components must be utilized with other components of the same supplier in order to function properly. (Campanini 409, 505; tr. 683–84 *in camera;* tr. 2677 *in camera;* Heller 4182.)

22. The record indicates that a certain amount of standardization of the wheelend hardware, or sensor, has occurred. As of late 1975, one OEM used an Eaton sensor in combination with Goodrich logics and valves. Two others used Eaton sensors [10] with Kelsey-Hayes logics and valves and one OEM combined Wagner sensors with Kelsey-Hayes logics and valves. (tr. 691 *in camera;* Deibel 1024; DeClaire 1079–80, 1110; Denholm 1684; tr. 2670–71 *in camera;* Megginson 4238; tr. 4365–65A *in camera.*)

23. Some witnesses expressed doubt that standardization of the sensor will ever be total due in part to the varying mountings required in different wheels. (Deibel 1024; Megginson 4250–51). Moreover, the signals fed from the sensor into the logic module generally differ among the various antiskid systems. (Campanini 409–10, 412; Megginson 4251.)

24. Complete standardization and separate sales of the logic modules and valves is even more unlikely for several reasons. Some manufacturers combine the valve and logic module into a single unit. (CX 190C; CX 191H, J; CX 194C; CX 196; CX 197; CX 198E–F; CX 199C; CX 204A; CX 550E; CX 556C; RX 149; tr. 692 *in camera;* Denholm 1712; Henry 2453; Bell 2672; Heller 4188; Polkow 4335–36.) In addition, manufacturers' valves perform different functions and have varying degrees of control incorporated within them. (CX 191K; CX 194B–C; CX 196; CX 197; CX 198H; CX 199C; CX 203B; CX 550D;

tr. 1710-11 *in camera;* Bell 2629; Megginson 4216-17, 4220-21, 4239-40, 4256-57; Deibel 1025.) On the other hand, the logics of certain manufacturers can be used with the valves of other manufacturers. (Dahl 4103; Denholm 1705.)

25. Some of the larger OEM's would prefer to buy standardized components. (Heller 4160-62.) For instance, International Harvester has been reviewing many competing valves for use with other manufacturer's sensors and logics. (Heller 4180-82.)

26. Witness Campanini, a representative of supplier Berg/Fiat testified that he expected standardization of the sensor, logic and valve, and that Berg/Fiat would eventually sell the logic and valve separately as well as together. (Campanini 523-24.) He felt that this standardization [11] would take place in 3-5 years for the sensor and another 3-4 more years for the valve. "I believe the standardization of components within the group of qualified manufacturers of components does provide an economy, and, as such, will be promoted by all concerned." (Campanini 523.)

27. However, a major factor reducing the possibility of a complete components market in antiskid is the desire by the vehicle manufacturers and ultimate users for single source responsibility should an antiskid device fail and liability ensue. (Lindquist 561-62; Deibel 1025-26; Bell 2629.)

28. The antiskid market, having been in existence only since 1975, was admittedly in a state of flux at the time of trial. (Perry 747; Henry 2455; Campanini 490; Reeve 891-92; Bachman 145-46.) Nevertheless, it developed as a systems market from the beginning and, at the time of trial still existed as a systems market. The standardization strived for by some OEM's had not yet been achieved. Basically, the seven manufacturers market the product as an integral device and the buyers purchase as such.

29. During 1975, sellers and buyers of antiskid devices participated in hearings held by NHTSA to determine whether FMVSS 121 should be suspended, revoked or modified. (Heller 4159-60; Campanini 488-489; McCuen 2070-71.) Throughout 1975, doubt existed as to whether FMVSS 121 would be administratively or judicially voided in whole or in part. (CX 585; McCuen 2070-71; Denholm 1701.) [12] Prior to becoming effective, it was repeatedly modified and delayed. (39 F.R. 20380; Deibel 1041-42). After it became effective, numerous modifications were proposed, commented on, and enacted. (39 F.R. 20380; 40 F.R. 1246; 40 F.R. 2989; 40 F.R. 38160; 40 F.R. 12797; 40 F.R. 8953; 40 F.R. 31771; 41 F.R. 1598; 41 F.R. 8784; 41 F.R. 29703; 41 F.R. 52055.)

30. In addition, in the beginning, the antiskid devices of several

manufacturers still had performance "bugs" which necessitated major recall campaigns during 1975. (Brown 1138; Campanini 491; CX 585.)

31. Notwithstanding the imperfections in the antiskid market, including its short, erratic past and uncertain future, it nonetheless constitutes a valid product market for Section 7 purposes, and as such merits further analysis. (Mann 5784.)

B. *Barriers to Entry or to Effective Competition*

1. Capital Costs

32. "Capital costs" measure the amount of money needed to build and equip a production facility of minimum efficient size, and includes the costs of inventory, working capital and, with respect to antiskid, research and development. (Mann 5684-85, 7563; Nelson 5819.) [13]

33. Various estimates of capital cost were given by supplier witnesses. This is because of variances on the part of suppliers in their methods of manufacture and/or assembly of the components. (Bell 2604; tr. 683 *in camera;* Denholm 1669, 1686-89; Deibel 1021; Campanini 373; DeClaire 1075-76; Vause 2211). Thus, the estimated capital costs ranged from several million dollars to $14.6 million. One company spent $14.6 million; another approximately $13 million; another less than $10 million; and one more estimate was several million dollars. (Deibel 1014-15; Brown 1123; McCuen 2074; Campanini 449, 457.)

34. Respondent's economic expert was of the opinion that capital costs fell into the moderate range. (Mann 5686, 7532). Complaint counsel's economic expert placed them on the borderline between moderate and large. (Nelson 6541.)

35. The record suggests that capital costs for entry might be lower today than they were for the present suppliers of antiskid. During the postponements and modifications of FMVSS, prospective suppliers faced continuing research and development costs to alter their designs and prototypes. (Brown 1146, 1177-78; Bell 2602-03.) An entrant today would not be charged with this added expense. Moreover, there is evidence in the record that development of a logic module is a less expensive task today than it previously was, since today's new entrant can use certain readily available parts. (Megginson 4241-45; Schimpf 4319.) [14]

36. Should the antiskid market ultimately develop into a components market, the capital costs for entrance into the production of a sensor, logic or valve would probably be lower than for

entrance as an antiskid "system" supplier. There was testimony that a logic module could be designed for $1 million or less. (Schimpf 4310.)

2. Absolute Costs

37. The absolute cost barrier for entrance into the antiskid market is low. (Mann 7573.) An absolute cost barrier exists when firms in an industry possess some advantage such as patents imposing upon new entrants a cost penalty such that the entrant would have a higher unit cost at the same level of output of existing firms. (Mann 5683.) There are presently no blocking patents in the industry which could deter entry or require a royalty payment. (Lindquist 584; Perry 744.) There is apparently no scarcity of essential raw materials or components needed to assemble the sensors, logics and valves. (DeClaire 1074; Campanini 421-22; Megginson 4244.) Unquestionably the development, testing and manufacture of the antiskid device require application of sophisticated electronic technology, automotive braking technology, and vehicle dynamics theory, but the costs of obtaining the required knowhow is the same for all firms in the industry. (Campanini 435-36, 453-54; tr. 689-90 *in camera;* Deibel 1012-14, 1026-27; Denholm 1673-74; Schimpf 4306.) New firms possessing technical competence could bid along with those established in the industry for the expertise required. [15]

3. Economies of Scale

38. Economies of scale represent the level of output or market share which a prospective entrant would need to achieve so as not to be at a unit cost disadvantage compared to existing competitors. If, in order to operate at a minimum efficient level, a firm must secure 10 percent or more of a market, then that market is characterized by a high economy of scale barrier. (Mann 5676-77.)

39. Antiskid suppliers testified that they equipped themselves for production of well over 10 percent of their estimate of the market. For example, one supplier built a facility to produce 30 percent expected unit sales; another built a factory capable of supplying 50 percent; one felt it needed 30-35 percent of the antiskid market to insure a decent return on investment; one supplier estimated that a firm needed 15-16 percent of the antiskid market in order to remain a viable competitor. (See tr. 676 *in camera;* CC's 1st RACF - #71; CX 248B; see also CC's 1st RACF - #96; tr. 2606-07 *in camera*). Still other suppliers indicated they needed 20-40 percent unit share to remain

in the market. (Brown 1144; see tr. 2450 *in camera.*) Another supplier testified that it needed 50 percent of the antiskid market in order to meet its profit goals. (Deibel 1017-18.) And two antiskid manufacturers testified that the antiskid market is very "volume sensitive." (Hess 5857, 5888; Brown 1153.)

40. While respondent contends such testimony is imprecise or non-determinative, it is clear that the presently competing antiskid systems suppliers believe that a market share of more than 10 percent is required. Consequently, this barrier to entry must be placed in the "high" category. [16]

4. Product Differentiation

41. A product differentiation barrier exists when an entrant must charge lower prices or spend extensively on sales promotion in order to attract away buyer loyalties from an established seller. Generally, in producers' goods markets this barrier is low, as knowledgeable purchasers make their decisions on a price/quality basis. (Mann 5678-79.)

42. The record indicates that antiskid suppliers believe it is helpful in marketing that a firm has a long established reputation for quality and performance in the automotive or heavy duty vehicle field. (Campanini 455-57; tr. 689-90 *in camera,* 713, 723-24 *in camera;* Deibel 1027; DeClaire 1082-83; Brown 1153-56.) During the developmental stage in particular, would-be antiskid suppliers felt that selection of their systems by a major OEM as "standard" would assist them in marketing to others and would enhance their credibility as a reliable source. (Perry 715; Vause 2220, 2236; tr. 2641-42 *in camera.*)

43. There is evidence in the record that antiskid suppliers believed it important in marketing the antiskid device to be able to provide an effective aftermarket distribution for parts and service. (CX 46, CX 68; CX 89D; CX 91A; CX 191-O; CX 200C; CX 244C-D; CX 550C; CX 546; CX 582A; CX 585G-H; Campanini 430, 457-58; Lindquist 566-67; Deibel 1011, 1057; DeClaire 1083; Brown 1153-55.)

44. The OEM's or buyers in the antiskid market are generally well informed, having participated actively in the testing and development of the antiskid system before implementation of FMVSS 121. (Mann 7567; Hulverson 4450-64, 4497-4510.) [17] When buyers are well informed about a product, they usually purchase on the basis of price and quality instead of product differentiation factors. (Mann 5792; Nelson 6546.) And there is testimony in the record that purchasers in fact did buy on the basis of price and

quality. (Dahl 4048; Allen 187; Campanini 487, 493; Bachman 145; Reeve 892.)

45. Thus, while the record indicates the presence of some product differentiation elements which must be taken into account to effect successful entry or to compete effectively, this barrier is not insurmountable.

C. *Anticompetitive Effects*

46. In 1975, Fruehauf's purchases of antiskid braking devices totaled $1,938,614 or 4.7 percent of the dollar universe. (Nelson 6530-31 *in camera;* Mann 7531; tr. 2616 *in camera;* Robins 2907.) In 1975, Kelsey-Hayes sold 32.5 percent of all units sold and 28.6 percent of total dollar volume. (CX 612A-B *in camera;* Campanini 470-72 *in camera;* tr. 695-6 *in camera;* tr. 1126-27 *in camera;* tr. 1292-93 *in camera;* tr. 2615-17 *in camera;* tr. 2906-07 *in camera;* tr. 4341 *in camera;* Nelson 6528-29 *in camera;* Mann 7531 - see CX 585C.)

47. The modification of FMVSS 121 which resulted in the elimination of antiskid devices on the front axles of trucks and truck tractors operates to decrease the total universe both in terms of dollars and units. This will serve to increase respondent's percentage of the total market purchases as Fruehauf manufactures only trailers. [18]

48. In 1973, prior to the effective date of FMVSS 121, Fruehauf began contacting several prospective suppliers of antiskid devices. (Perry 708, 755-58; Hess 5859; tr. 5998, 6034 *in camera;* tr. 2634-44 *in camera.*) Fruehauf had decided that it wanted an in-axle sensor design and communicated this desire to its potential suppliers. (CX 89C; CX 91A-B; Perry 711; Vause 2216; Hulverson 4460-63; Hess 5905; see Deibel 1035-36; tr. 2666 *in camera;* Megginson 4202; see CX 246B.)

49. As of August 1973, competitors of Kelsey-Hayes did not consider it a likely candidate to become a standard supplier of antiskid devices to Fruehauf, primarily due to Kelsey-Hayes' lack of an in-axle sensor design. (CX 239L *in camera;* CX 693B *in camera;* CX 695 *in camera;* Perry 710-11, 713, 752; Deibel 1035; tr. 2644, 2667 *in camera;* Hess 5857, 5864, 5889-90, 5905; see Vause 2218; Hulverson 4478A.) In fact, as of August 1973, Kelsey-Hayes was not and knew it was not an approved antiskid supplier to Fruehauf because of its lack of a proven in-axle sensor. (CX 583A-D; Vause 2218-19; Hulverson 4478A.)

50. Because of Fruehauf's acquisition of Kelsey-Hayes in October 1973, Kelsey-Hayes competitors believed that it would get at least a part of Fruehauf's patronage, and expressed their concern to

Fruehauf. (CX 239L *in camera;* Campanini 513; Deibel 1036–37; Brown 1147; Rowan 1935; Hess 5864, 5887; see Perry 713; Widell 2682; see CX 697B *in camera.*) A witness from Rockwell felt that all other antiskid suppliers would be effectively foreclosed from the Fruehauf business because of the acquisition. A B.F. Goodrich witness testified that Fruehauf's acquisition of Kelsey-Hayes "made it more difficult for the B.F. Goodrich Company to get a portion of that business." (Hess 5887; see tr. 6084 *in camera.*) A Wagner memorandum stated that "obviously our potential for selling [19] the skid control system to Fruehauf which we have been developing for such a long time is seriously impaired by the potentiality of a Kelsey-Hayes/Fruehauf merger." (CX 239L *in camera.*)

51. Buying "in-house" is a recognized corporate policy of Fruehauf. (Dahl 4110.) Although this policy has been questioned from time to time, it has been decided at the corporate management level that company-manufactured products are to be utilized despite the fact that it might sometimes be more economical to purchase from outside sources. (Dahl 4110–11; Reghanti 5463.)

52. Antiskid units purchased by Fruehauf from "standard" suppliers bear the Fruehauf brand name rather than the name or brand of the supplier. (Deibel 1035; Rowan 1907, 1917–18; Bell 2630). For example, the physical exhibit which was referred to by Kelsey-Hayes employees as a Kelsey-Hayes' in-axle sensor was branded "ProPar." (RX 222A–C.)

53. Fruehauf selected no antiskid supplier as "standard" until January 1974. (CX 240A–B; Rowan 1918, 1923.) The two suppliers selected were Kelsey-Hayes for dry freight vans (50 percent of production) and Wagner for other vehicles such as dumps, tankers, platform trailers and all Fruehauf "Hobbs" brand trailers (50 percent of production). (CX 240B; Perry 710; Rowan 1918; Bell 2631; Hess 5888; see Hulverson 4476.)

54. It should be noted that additional vertical foreclosure exists in the antiskid industry by virtue of General Motor's ownership interest in AC, one of the seven antiskid suppliers. (Brown 1137; tr. 1294 *in camera;* tr. 2619 *in camera;* tr. 2906–09, 2978, 2982–83 *in camera.*) [20]

55. As for potential entry into the antiskid market, Bendix has the ability to enter as a "system" or component supplier. (Perry 680; Deibel 1020; Denholm 1673; Bell 2610.) The large OEM's such as Ford and International Harvester also have that ability. (Campanini 515; Deibel 1049; DeClaire 1108–09; Heller 4163, 4183, 4186; Megginson 4242–43.)

56. There was testimony that Bendix may in fact attempt to

enter the antiskid market. (Perry 677–79; DeClaire 1082; Brown 1153; Bell 2610–11.) As of November 1975, Bendix was operating at the research and development prototype level with regard to producing the device. (Henry 2439.) On the other hand, Ford was considered qualified by industry members but unlikely to enter. (Deibel 1049; DeClaire 1108; Brown 1154–55.) International Harvester was viewed as unlikely to enter due to its limited in-house requirements and its lack of in-house electronics capability. (Deibel 1049; Brown 1154–55, 1165.)

57. Subcontractors who produce one or more components of an antiskid system are generally not perceived as competitors or potential competitors by present systems suppliers. (Campanini 517; tr. 688 *in camera;* 763; DeClaire 1118–19; Denholm 1704.)

58. Components subcontractors are not permitted to sell to other customers the products which they manufacture for the antiskid systems suppliers. This is because the components are of a proprietary design owned by the antiskid suppliers. The tooling used to manufacture such components is also owned by the suppliers. (CX 316I; CX 318F; CX 319E; CX 324V; CX 448D *in camera;* tr. 688, 738 *in camera;* Deibel 1021–22; MacDonnell 2043; Megginson 4242; Schimpf 4297, 4313.)

59. It would also require a significant amount of development and testing over an extended period of time in order for an antiskid subcontractor to be in a position to offer a component for sale directly to an OEM or ultimate user. (Perry 763; Schimpf 4306, 4309–10.) [21]

VI. TRUCK TRAILER MARKET

60. There is no dispute and it is found that truck trailers as a whole constitute an appropriate product market within which to judge the competitive effects of the merger. (See admission of respondent's counsel tr. 13; Mann 5749.) Indeed, the existence of this market has been recognized by the Commission in prior cases, most recently in *The Budd Co.,* 86 F.T.C. 518, 572 (1975). See also *Fruehauf Trailer Co.,* 67 F.T.C. 878, 904–05, 937 (1965).[1]

61. Truck trailers are unique products for which there are no substitutes. A truck trailer is a nonpower vehicle designed to be pulled by a power vehicle, known as a tractor, for the purpose of transporting or hauling products over the highway. (Bachman 70–

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[1] The respondent's horizontal acquisitions in the mid-1950's of two competing trailer manufacturers, Strick, the third largest in trailer sales, and Hobbs, the sixth largest, were found to be a violation of Section 7. The Commission ordered divestiture of both companies, but later modified its order allowing respondent to retain Hobbs. See 69 F.T.C. 180 (1966).

71.) It consists of a chassis or frame on wheels and a body attached to the frame. (RX 265; Bachman 96-97.)

62. There are many types of trailers, including van, platform, tank, bulk commodity and dry materials, pole and logging, dump, low-bed heavy haulers, van size container and container chassis. (Complaint and Answer, Para. 4; CX 584G, H, I, L, N, O; CX 660J-M; RX 35D, T, U, X; Bachman 71-72, 96-97; Allen 172; Stein 328; Reeve 852; Fontaine 3548.)

63. The truck trailer industry is recognized as a separate economic entity. (Reghanti 5231-32.) There is a national organization, The Truck Trailer Manufacturers Association, to which many truck trailer manufacturers belong. (Allen 175; Stein 330-32; Fontaine 3558.) There are magazines which focus specifically upon the truck trailer industry. [22] (CX 561A-B; Fontaine 3548-49). The Bureau of the Census reports truck trailer shipments separately and the information is utilized by truck trailer manufacturers in the conduct of their business. (CX 254A-L; Bachman 44-45; Allen 174-75; Stein 330-32; 351-52.) R.L. Polk Company, a statistics gathering organization, reports information on overall registrations and on customers of truck trailers, which information is also used by the manufacturers of truck trailers. (Reghanti 5231-32.)

64. Truck trailers have peculiar characteristics and uses. (CX 584G, H, I, L, N, O; CX 660J-M; RX 35D, T, U, X; Bachman 71-72; 96-97; Allen 172; Fontaine 3548.) Their manufacture requires unique production facilities. (Complaint and Answer, Para. 4; Bachman 27; Allen 176-77, 189; Stein 337; Dahl 4056; Flagan 5052-53.) There are distinct customers for truck trailers. (Bachman 18-19, 100; Reeve 852.) Truck trailers have distinct prices. (Bachman 45-46; Reeve 870, 900; Bell 3308; Kortenhaus 3531.) They are sold through specialized vendors, *i.e.*, company based sales personnel, company-owned branch sales outlets or independent distributors of truck trailers. (Bachman 22-23; Allen 189; Reeve 856-57; Fontaine 3567.)

A. *Market Structure*

65. There are numerous manufacturers of truck trailers in the United States (Stein 351; RX 285M-R; CX 254A), and industry witnesses knew of no significant imports from other nations. (Bachman 20; Allen 173; Stein 336, Reeve 870.) There were, however, some exports. (Bachman 156-57.)

66. Total value of truck trailer shipments in the United States is in the area of $1 billion per annum (CX 254A) and concentration in this market is high. According to 1972 Census data, the top [23] four

firms accounted for 55.0 percent of shipments and the top eight 69.3 percent.[2] The 1973 figure for the top four and top eight firms were 54.5 percent and 70.4 percent respectively. Many of the top twenty firms and all of the remaining firms have market shares of less than 2 percent or 1 percent. (See RX 266.) The concentration levels in the market have remained fairly constant over the last ten years. For the years 1968 to 1971, inclusive, the combined market shares of the top firms have been as follows:

	Top Four	Top Eight
1968	54.6%	68.4%
1969	58.0	70.8
1970	51.2	65.1
1971	48.6	63.8

67. Throughout this period Fruehauf has been the largest manufacturer in the industry with a 1973 market share of 25.2 percent. And for the period 1968-72, it had shares of 29.9 percent, 32 percent, 26.4 percent, 24.9 percent and 24.4 percent respectively.[2]

68. Respondent points out (using figures from unadjusted Polk registrations), top four and top eight firm concentration has declined over the 19-year period 1955-73 and the share of market held by the largest companies has shrunk. (Mann 5752; RX 266.) During this time, according to Polk data, Fruehauf's market share slipped 17.9 percent, from 41.1 percent to 23.2 percent. (RX 266.) Fruehauf's largest competitor, Trailmobile, also lost market share over this period. (Reghanti 5315; RX 266.) Fruehauf's President and Chief Executive Officer, Mr. Rowan, testified, but [24] presented no supporting data, that the company's market share has continued to decline; and that in September of 1975 its share was 19 percent. (Rowan 1974, 2002.) It should be noted that there has been little change in the identity and market position of the top eight firms in the industry since 1955. (RX 266, Reghanti 5317.)

69. The figures relied upon by respondent show that certain small and medium-sized companies have increased their market shares (RX 266), but only by small incremental amounts. Gains against Fruehauf have been made largely by top eight firms.

70. The truck trailer market has been growing at the rate of about 8 percent to 10 percent per year, (Bachman 80), and there has been some new entry into trailer manufacturing and sale. (Bachman 129-31.)[3]

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[2] See chart at p. 75 of complaint counsel's proposed findings, *in camera*, for compilation of percentages referred to in this paragraph.

[3] Monon, for example, was not in business in 1967-68. (Reghanti 5262.) Monon has been successful in selling to

(Continued)

71. The manufacture of truck trailers can range from an assembly operation that requires relatively inexpensive machinery and unskilled labor to vertically integrated, mass production facilities.

72. There was testimony that competition in the truck trailer market is on the basis of price and quality, and the ability to meet customer specifications. (Reghanti 5377-80; Alderson 5927; Reeve 874; Bachman 107-08; Bell 3345; *see also* Kortenhaus 3511-12.)

73. Trailer prices declined from 1950 to 1971; they have increased somewhat since then due to increases in material and labor cost and the government required FVMSS 121 antiskid system. (Bachman 138, 154; Reeve 900; Reghanti 5396.)

74. Trailer prices have increased less than have prices in general over the period 1967-74 (RX 233), while the quality of trailers has generally improved. (Bell 3301.)

75. Many customers are sophisticated and knowledgeable about the trailers they are purchasing. The major truck trailer purchasers are large fleets, which typically have maintenance and engineering staffs which maintain detailed records of performance of trailers and their components. (Bachman 104-05; Bennett 267; R's 1st RAF - #124.) In the truck trailer market, bids are often made with regard to specifications presented by customers. (Bachman 106; Bell 3312; Pfund 3372; Cox 3456; Kortenhaus 3509; see also Stein 358.)

76. Few fleets are standardized on any one trailer, and the make-up of a fleet may well vary over time. (Rowan 2005; Bachman 107.) Most fleets contain trailers built by several manufacturers. (Rowan 2005; Cox 3455-56; Alderson 5914, 5926; Bell 3344; Kortenhaus 3508; Pfund 3370.) There are fleets composed of trailers made by the largest down to the smallest manufacturers. (Bachman 110.)

77. Some large fleets have the capacity to build their own trailers (Bell 3306; Cox 3478), and some do so now, albeit infrequently, or have done so in the past. (Reghanti 5310-11, 5314, 5434-36; Thompson 3430, 3439-40; Cox 3481-82.) Although some fleets have rebuilding capabilities (Kortenhaus 3516-17; Thompson 3422), fleets have not entered the manufacturing market because it has been economically sounder for them to purchase than to build their own trailers. (Cox 3498; Bell 3306.) [26]

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major fleets, including Saunders (Cox 3455-56, 3491-92), Mason & Dixon (Reghanti 5384), and Yellow (Alderson 5914). One industry witness said Monon was not a substantial, but an effective, competitor. (Bachman 129-30.) Bertolini has entered the truck trailer market since 1968. (Bachman 40-43.) Stainless Tank & Equipment, a former repair facility, entered the truck trailer market within the past four or five years manufacturing tanks for Coca-Cola. (Allen 175.) Polar was also a rebuilder before entering the trailer market. (Allen 210.) [25]

B. *Barriers to Entry or to Effective Competition*

1. Capital Costs

78. According to respondent's economic expert witness, Dr. Mann, the capital cost barrier into the truck trailer market is low or nonexistent. He felt that all estimates in the record fell into Bain's "small" category, (adjusted for inflation), that is, below $4 million or touching $4 million.

79. One witness did testify that the production of truck trailers could be entered and 2 percent of the market captured for an investment of $3-4 million but the witness felt his estimate was "really incomplete" in that he had estimated the lowest possible figure of $2 million for building vans using leased facilities, that is, for making a "poor boy" entrance into the market. (Reghanti 5308-09.)

80. Respondent maintains that numerous truck trailer manufacturers have entered with an investment of less than $2 million including Monon, Kentucky, Utility, Transcraft and Ohio Body (Reghanti 5309-10), and that numerous manufacturers have entered and survived for many years with market shares of less than 2 percent. (See RX 266.)

81. One witness was of the belief that entry into the production of tanks could be accomplished for $3-4 million. (Allen 198.)[4]

82. It is the position of complaint counsel, however, that effective competition in the truck trailer market requires more than a single plant, and that therefore, the capital cost barrier is in the $15 million range, which is on the borderline between a moderate and large barrier to entry. (Nelson 6567.)

83. One witness estimated the cost of replacing one of its tank trailers plants at $10 million. (Allen 176-77.) Others placed the cost of a dry freight van plant at between $6 million and $8 million. (tr. 908 *in camera;* Dahl 4064; tr. 5485 *in camera.*)

84. In addition to the cost of a plant, a truck trailer producer must have several million dollars invested in inventory and receivables. (Allen 197; Fontaine 3591-92.)

85. Generally, a firm must have more than one plant in order to gain the advantages of offering a fuller line of truck trailers, and there are distinct advantages to manufacturing and selling as full a

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[4] There was testimony that for the most advantaged potential entrants, the large fleets and body shops (Reghanti 5311), the cost would be less. For example, PIE could enter truck trailer production for "thousands of dollars." (Bell 3355-56.) Several fleets have made trailers for their own use in existing repair facilities. (Reghanti 5310-11, 5314; Thompson 3430, 3439-40; Cox 3481-82.) Other fleets are capable of doing the same. (Bell 3306; Cox 3478.)

line of truck trailers as possible. (Bachman 17; Bennett 225; Reeve 901; Rowan 1905; Reghanti 5314-15.) [28]

86. There was testimony that a full line of truck trailers:

(a) enhances the ability to sell certain customers by allowing the full-line manufacturer to satisfy all the customers' needs rather than a part of them (Bachman 17-18);

(b) enables the manufacturer to obtain manufacturing efficiencies by combining certain types of production equipment (Bachman 18); and

(c) enables the manufacturer to gain sales efficiency since his sales force can sell the broader line with little added marketing cost thus spreading distribution costs out over more items of manufacture (Bachman 17; Bennett 227; Rowan 1906).

87. Fruehauf has the most complete line of trailers in the industry, and as such has the opportunity to generate greater volume. (Rowan 1905-07; Reghanti 5314.) Trailmobile is the only other trailer manufacturer comparable to Fruehauf in size and product line. (Rowan 1905-06; Reghanti 5315.)

88. There is a labor cost advantage in producing a single type of trailer in a single plant as against producing a variety of trailers in that plant. (Flagan 5055.) Fruehauf's Avon Lake plant which produced a full line of trailers, was closed, because higher labor costs at Avon Lake as compared to other Fruehauf plants with a less broad product line made it uneconomical to produce a full line of trailers in this one plant. (Flagan 5050-55.) Subsequent to the Avon Lake experience, Fruehauf concentrated on setting up new, smaller plants specialized in the production of a single product line. (Flagan 5051.) [29]

89. There was evidence that truck trailer manufacturers typically produce different types of truck trailers in separate plants. Thus:

(a) Great Dane, primarily a van trailer manufacturer, has its tank trailers manufactured by Ohio Company at its plant in Edgerton, Wisconsin (Reeve 873, 901);

(b) Fontaine has a special plant for production of bulk commodity trailers in Birmingham, Alabama which is separate from its platform and special trailer production plant in Haleyville (Fontaine 3591);

(c) Great Dane produces van trailers in certain of its plants while its subsidiary, Arrow produces platform trailers in a different plant (Reeve 852);

(d) Fruehauf's Charlotte, North Carolina plant produces only van trailers (Dahl 4138-39); and

(e) Kentucky specializes in furniture vans in its plant (Reeve 910).

90. An additional reason for multiple truck trailer manufacturing plants is to achieve geographic dispersion. Most of the major truck trailer manufacturers have more than one plant. (Bachman 21; Bennett 274; Dahl 4059.) Fruehauf has 11 truck trailer manufacturing plants located throughout the country. (Complaint and Answer, Para. 4; CX 37M; CX 584L, Z-11; CX 660; Flagan 5170.) Heil has two truck trailer manufacturing plants; one in Milwaukee, Wisconsin and one in Lancaster, Pennsylvania. (Allen 176). Utility has truck trailer manufacturing plants located in Utah, California and Texas. (Bennett 252). Trailmobile has at least two truck trailer plants; one located at Cincinnati, Ohio and one at West Point, Pennsylvania. (Dahl 4059.) Great Dane has three plants located in Savannah, Georgia, Memphis, Tennessee and Brazil, Indiana. (Reeve 872.) Strick had five [30] truck trailer plants throughout the United States in 1972 but is phasing out and changing the make-up of several plants. (Bachman 20-21.) Prior to its exit from the business, Brown had at least two plants located in Hammond, Indiana and Reading, Pennsylvania. (Reeve 900-01.)

91. The ability of a truck trailer manufacturer to compete for sales in a particular geographic area may be determined by whether or not it has a plant located in that geographic area. Utility, which has plants in California, Utah and Texas sells primarily in the western United States. (Bennett 227.) Great Dane built a plant in Brazil, Indiana in order to be able to serve the midwestern market. (Reeve 872.)

92. Fleet purchasers such as PIE, UPS, Saunders Leasing Company and North American Van Lines prefer to purchase trailers from nearby plants in order to save on the cost of transporting the trailers from the manufacturer's plant to the point on the fleet's line where the trailer is to be put into service. This is a major consideration in the purchasing decision. (Bell 3353; Pfund 3389, 3400; Thompson 3419; Cox 3457.)

93. There was testimony that the building of a new plant in a particular geographic area near a fleet's line gives the trailer manufacturer an enhanced opportunity to bid on that fleet's business. For example, PIE will give Comet the opportunity to bid on bulk commodity trailer sales to it because Comet built a new plant near Chicago in close proximity to PIE's line. (Bell 3362.)

94. Accordingly, the testimony is convincing that more than a single plant at a single location is needed in order to offer effective competition to the leading firms in the truck trailer industry. The capital costs involved in this respect are thus substantial. [31]

2. Absolute Costs

95. Respondent is of the belief that the absolute cost barrier to entry into the truck trailer market is low. (Mann 5758.) Even the Commission's economic expert describes this barrier as low to moderate. (Nelson 6569.) Neither the existence of patents nor scarce natural resources, the two normally significant absolute cost barrier factors, are involved in this market. (Nelson 6567, 6811-12; Mann 5757-58.)

96. A truck trailer is a comparatively uncomplicated piece of equipment whose manufacture requires basically an assembling of components. (Stein 337; Flagan 5078; Reghanti 5297.) The components are generally available for purchase from a variety of sources (Dahl 4057; Reghanti 5310), and no great amount of labor is necessary for assembly. (Dahl 4057.) Nor is highly sophisticated equipment essential for this operation. (Flagan 5044, 5048.)

97. While opportunities for technological improvements on truck trailers can be described as somewhat limited,[5] some patents have been obtained by Fruehauf. But, according to respondent's officials, competitors have been easily able to circumvent them, as in the case of Fruehauf's roller [32] and floor welding patents (Reghanti 5297, 5299; Flagan 5087, 5165).[6]

98. While the record discloses no scarcity of natural raw materials, shortages of necessary component parts such as wheels have in fact occurred. (Nelson 6567-68.) In such cases, it would naturally be advantageous for a trailer manufacturer to have an assured source of supply for the scarce components, such as might occur if a trailer manufacturer were vertically integrated into wheels. This would also minimize financial losses associated with discontinuance of production. (Allen 184-85, 188; Stein 342, 346; Reeve 855-56, 860-62; Smith 989; Rowan 1904; Fontaine 3578-81; Reghanti 5303.)

99. Fruehauf manufactures all of its own trailer components except wheels (excluding Kelsey-Hayes production), tires, electrical systems and some of the flooring. (Bachman 28; Rowan 1895.) Respondent has a higher degree of vertical integration than any of its competitors and its vertical integration has embraced more

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[5] Opportunities for improvement are limited by government restrictions on length, height, width, weight, load on axles, load on highway, and connection between tractor and trailer. (Flagan 5079-80; Reghanti 5297).

[6] Contributions to trailer technology have not been limited to Fruehauf; innovations have been made by other manufacturers such as Utility, Venema & Wiggers, Strick, Hackett, Timpte, and Theurer. (Bachman 93; Bennett 261-62, 264; Flagan 5083-84.) Strick, for example, views its innovations as one factor for its success and growth in recent years (Bachman 95); and one witness felt that in the Los Angeles area, increasingly specialized equipment produced by manufacturers other than Fruehauf has been entering the market. (Goedhart 3795-96.) Some components suppliers have also introduced improvements. (Bennett 313.)

components than anyone else in the industry. For example, Fruehauf is the only truck trailer manufacturer with its own axle and aluminum plants. And axles and aluminum are two of the major cost items in the manufacture of truck trailers. (Rowan 1898–99.) [33]

100. The component parts which Fruehauf itself manufactures include:

(a) assembled axles (CX 561A–B; Bachman 28; Dahl 4107; Flagan 5138);

(b) aluminum sheet and extrusions for body parts and other components, such as extruded aluminum rivets (CX 561A–B; Bachman 28; Dahl 4108; Flagan 5138, 5167);[7]

(c) laminated wood flooring (Bachman 28; Flagan 5139);[8]

(d) suspensions and suspension shafts (CX 547; CX 561A–B; Bachman 28; Dahl 4108; Flagan 5144);

(e) brake shoes and all other braking components on the axle except the brake drum and air chamber (Bachman 28; Flagan 5140); [34]

(f) steel stampings (Bachman 28);

(g) underconstruction (Flagan 5139; Reghanti 5298);

(h) landing gear or support leg assemblies (Bachman 28; Flagan 5138, 5144; Reghanti 5298);

(i) running gear (Bachman 28);

(j) upper couplers (Flagan 5143; Reghanti 5298);

(k) door hardware including door lock rods (CX 561A–B; Flagan 5138–39);

(l) protrusion-formed plastic components (Flagan 5138);

(m) I-beam cross members (CX 516A–B);

(n) cam shafts and cam shaft supports (Flagan 5140);

(o) slack adjustors (Flagan 5140);

(p) hitch assemblies (CX 561A–B); and

(q) sand shoes. (Flagan 5067).

101. According to its officials, Fruehauf's degree of vertical integration gives it the opportunity to better control production cycles and scheduling of materials as required, the ability to control in-plant inventories and minimize inventory levels at assembly

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[7] Sheet aluminum is the most commonly used van trailer side and top material. (CX 544A). Fifteen to 20 percent of the cost of a typical aluminum exterior post van trailer is for aluminum sheet and aluminum extrusions. (Bachman 30.) Fruehauf entered the aluminum business in the mid-50's by constructing an aluminum extrusion plant in Decatur, Alabama. Subsequent to that, Fruehauf entered into a 50–50 joint venture with AMAX (American Metal Climax) to produce sheet aluminum. (Rowan 1898.) Fruehuaf obtains in excess of 90 percent of its aluminum extrusion requirements from its Decatur aluminum plant. The same is true for rolled sheet aluminum. (CX 544B; Rowan 1900.)

[8] Fruehauf acquired Montgomery Laminating Company in 1964 or 1965. It is a manufacturer of a special type of flooring and from time to time supplies Fruehauf with 10 to 15 percent of its flooring requirements. (Rowan 1899–1900; Flagan 5139.)

plants by maintaining one central inventory; the opportunity to control component quality, and to have additional profit centers. (Rowan 1904; Reghanti 5303.) [35]

102. There was testimony by industry witnesses that in order to vertically integrate into the manufacture of wheels and other truck trailer components, a manufacturer should have and most manufacturers do not have, both the financial resources for such production and the volume of truck trailer production necessary to support the required investment. (Bachman 34, 61; Allen 178, 185–86, 188; Stein 338, 342, 346; Reeve 855–56, 868; Fontaine 3597.)

103. Other than Fruehauf, truck trailer manufacturers including the largest ones, generally are either not vertically integrated into component parts manufacture or are only integrated to a limited extent. (Bachman 31; Allen 177; Bennett 228–29; Stein 337; Reeve 854–55; Dahl 4065–70.) Indeed, some truck trailer manufacturers merely assemble component parts which are purchased from outside sources. (Fontaine 3568.)

3. Economies of Scale

104. The expert testimony differs regarding the economies of scale barrier into the truck trailer market. Respondent's expert views this as low or unimportant (Mann 5759–60), while complaint counsel's expert places it in the moderate range.

105. Respondent contends that economies of scale can be obtained with a market share of less than 4 percent, pointing out that Fruehauf's plant built in 1969 in Charlotte, N.C. had the capacity to produce 24 trailers per shift, accounting for approximately 4 percent of trailer demand (Dahl 4138), and that both economists agreed that the Charlotte plant was efficient. (Nelson 6570–71; Mann 5759–60.)

106. To bolster its position respondent points to the fact that the top 20 firms include a substantial fraction of trailer companies in existence during the entire period 1955–73 with very small market shares of one or two percent. (RX 266.) It argues [36] that if economies of scale were a major technological characteristic of the industry, it would be unlikely that such small firms could exist over that period of time. (Mann 5759.) Notwithstanding, I find the complaint counsel's contention to be the more rational.

107. More than a single plant operation is required because of the need for a geographic dispersion of plants in order to attract the more proximate purchasers, and to obtain the competitive advantages of offering a full line of trailers. (Nelson 6571.) Accordingly, the 4 percent of industry production accounted for by one efficient plant

would not be the answer to the economy of scale question, as it would take at least two, and probably more plants of an efficient size to achieve the necessary geographic and the desirable product line coverage. (Nelson 6572.) This would place the economy of scale barrier in the 5 percent-10 percent or moderate range.

108. The existence of single plants or firms with limited production and limited market penetration does not prove that the economy of scale barrier in truck trailers is low. One or a few trailers at a time can be assembled in a small building, or a fleet maintenance facility of a manufacturer's sales and service branch operation. (Thompson 3430, 3439-40; Cox 3478, 3481; Dahl 4061; Reghanti 5306-07, 5311, 5313-14, 5430.) However, these installations cannot be efficient sized plants; otherwise, it would be illogical for trailer manufacturers to build the multimillion dollar plants which they have built. (Nelson 6570-71.)

109. Complaint counsel argue that order sizes and delivery schedules imposed on truck trailer manufacturers by the large fleet customers indicate the existence of economies of scale. A large fleet consists of anywhere from 100 to 10,000 or more truck trailers. (RX 262; RX 263; Bachman 36; Stein 329; Reeve 853; Pfund 3368; Thompson 3412-13; Cox 3455; Kortenhaus 3507; Dahl 4125; Alderson 5913.) And these customers [37] typically place orders for a substantial number of trailers at one time, often in the range of 100-700 units. (Bennett 271; Bell 3353; Pfund 3383-84; Thompson 3435; Cox 3461.) However, the fleets do not take delivery all at once; rather they establish intervals for a set number of trailers to be delivered per week or per month. (Bachman 108-10; Bell 3354; Pfund 3384, 3399-3400; Thompson 3435-36.)

110. The ability to produce the required amount of truck trailers within the set delivery period is often a major factor in a fleet's determination of which truck trailer manufacturer will obtain an order. (Bachman 107-10; Bell 3354-55, 3364; Thompson 3435-36; Cox 3494-95.)

111. There are a limited number of truck trailer manufacturers who can fill orders of the size that large fleets place within the set delivery schedules. (Bell 3354; Thompson 3436.) Unless the trailers are of a highly specialized type, the smaller trailer manufacturers are not normally looked to in the bidding because of their inability to meet delivery schedules. (Bachman 108-10; Fontaine 157-58.)

4. Product Differentiation

112. As a general rule, product differentiation as a barrier to entry has been found in consumers' goods markets rather than in

producers' markets, such as the truck trailer industry. (Nelson 6823-24.) And according to respondent's economist, at least, the record suggests that trailers are like any producers' goods industry; that there simply is no product differentiation advantage. (Mann 5766.) But the record discloses the existence of certain "special factors" involved in the selling of truck trailers. For purposes of analysis both expert [38] economist witnesses assigned these factors to the product differentiation entry barrier. These are (a) mass product capability, (b) vertical integration, (c) sales and service centers, (d) ability to accept trade-ins and (e) captive finance companies. (Nelson 6573; Mann 5754-55.)

(a). Mass Production

113. As noted above, some truck trailer customer demands impose a mass production requirement on manufacturers to meet large delivery schedules. Many truck trailer purchasers, including large fleets, place substantial orders for production of truck trailers with a given manufacturer and require the completion and delivery of those trailers within a set period of time. And the ability to meet these delivery schedules imposed by the purchaser is a prime factor in determining what manufacturer will receive the order.[9]

114. However, respondent maintains that sales records show that Fruehauf's penetration of sales to large fleets (those operating 500 or more trailers) is smaller than its penetration of overall trailer sales. (RX 258; see also Rowan 2005.) Complaint counsel [39] counters that there are very few fleets operating with 500 or more trailers.

115. Respondent contends that it is rarely necessary for a truck trailer manufacturer to deliver large numbers of trailers in a short period of time, as there are few very large orders.[10]

116. Delivery schedules are worked out on the basis of the capacity of the trailer manufacturer (Pfund 3384), and there was testimony that small manufacturers such as Alabama, Fontaine, Great Dane, Ohio Body, Monon, Dorsey and Pines have been able to meet the schedules. (Cox 3462-64; Alderson 5932). It is also not

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[9] In the early and mid-1950's, Fruehauf was engaged in the mass production of trailers at its Avon Lake, Ohio, plant. (Reghanti 5305.) The cost of producing a trailer was reduced fairly substantially at smaller plants as compared to Avon Lake, and that facility was therefore obsoleted and closed. (Flagan 5051.) Fruehauf plants today are of much smaller size and are not capable of mass production in the sense Avon Lake was. (Reghanti 5306.) This does not mean, however, that respondent's present manufacturing facilities are not capable of handling the orders of large customers, only that plants of the size of Avon Lake are not required.

[10] It cites statistics indicating that of the nation's 241 largest customers, 107 purchased an annual average of fewer than 100 trailers during 1969-74; 66 purchased an annual average of between 100 and 200 units; 28 purchased an annual average of 200 and 300 units, 14 purchased an annual average of between 300 and 400 units; and only 26 purchased an annual average of 400 or more units. (RX 188 A-250.) It reminds us that even these purchase averages are inflated by the aberrationally high volume of orders in 1974, when total registrations reached approximately 180,000 units. (RX 193.)

uncommon to split large orders between two or more manufacturers. (Bachman 109-10; Bennett 270-71; Cox 3461; Alderson 5933.)

117. The record shows that large fleets often do not buy standard production line trailers. (Cox 3459; Bachman 106; Bell 3312; Pfund 3371-72; Reghanti 5381-83), but usually maintain detailed service, repair and replacement records on trailers and trailer components in their fleets (R's 1st RAF - #124), and prepare specifications, such as CX 614A-C, based on this experience when ordering trailers. (Bachman 105-06; Bell 3308, 3312, 3319; Pfund 3374-78; Thompson 3419-20, 3448; 3460-61; Kortenhaus 3511-13, 3522-24, 3536-37.) This practice is often referred to as "specing." [40]

118. In specing, purchasers are concerned not merely with initial price, but with the total cost of the vehicle and its components over operating life. This overall cost includes initial price, cost of service and related downtime, and residual value when traded. (Bachman 110-11; Thompson 3445-46; Kortenhaus 3511-13; Cox 3459-60.)

119. There was testimony that smaller manufacturers are in a position to compete vigorously against Fruehauf in particular instances or circumstances involving speced sales to fleets. (Allen 203; Stein 359; Reghanti 5384-85, 5387; Pfund 3371-72; Thompson 3418-19; Cox 3455-56, 3484-85; Reeve 874.)

(b). Vertical Integration

120. Fruehauf is highly vertically integrated into the manufacture of component parts for truck trailers; its degree of vertical integration is greater than that of any other truck trailer manufacturer.

121. It manufactures a great many component parts which are unique and not interchangeable with the parts used by other manufacturers. (Bachman 24, 30; Bennett 239, 249; Stein 349-50.) Mr. Stein of Ohio Body explained that a large fleet "speced" Fruehauf parts on an order because they had always used Fruehauf and had Fruehauf repair parts. The price of the trailer had to be increased accordingly.

122. Fruehauf "ProPar" axle assemblies are a good example of this. (Bachman 30; Bennett 256-57; Rupert 815; Clem 2726-27; Bell 3321; Flagan 5149.) The brake components manufactured by Fruehauf are peculiar to Fruehauf's axle and are likewise not interchangeable with the corresponding components on other axles except in minor cases. (Flagan 5140.) [41] Fruehauf also manufactures portions of the undercarriage and a sand shoe of its own design. The sand shoe, however, is interchangeable with other manufacturers' designs. (Flagan 5067, 5144.)

123. Fruehauf also purchases unique components that are not used on competitive trailers. (Flagan 5162-63.) Standard wheels supplied by Fruehauf (and also by Trailmobile) on its trailers have a peculiar design which makes them non-interchangeable with wheels made by other manufacturers. (Stein 350; Mitchell 2520-21; Clem 2626-27.) The private label antiskid systems which Fruehauf supplies on its trailers have a peculiar design for application inside Fruehauf's tube type axle which make them non-interchangeable with antiskid devices made by other manufacturers. (Rowan 2036.)

124. Fruehauf's ProPar Division sells component parts which Fruehauf manufactures to other truck trailer manufacturers and to the aftermarket. (CX 547; Bennett 229; Rowan 1897; Reghanti 5491.) Fruehauf's ProPar parts are sold primarily to other truck trailer manufacturers but they are also sold through Fruehauf branches and through independent service shops. (Rowan 1897; Reghanti 5488, 5491.)

125. Fruehauf advertises its ProPar parts to prospective customers and attempts to persuade them to specify ProPar parts when purchasing Fruehauf or other makes of trailers. Fruehauf also urges trailer users to utilize ProPar parts for replacement or aftermarket requirements. (Bennett 236.) In 1975, more than 50 trailer manufacturers purchased ProPar axles for use as original equipment. (CX 660M.)[11]

[42] 126. Because fleets desire to standardize the truck trailer replacement parts in their inventory, once a manufacturer becomes a supplier to the fleet, the fleet is likely to remain with that manufacturer's part. (Bell 3351; Stein 349-352.) Fruehauf, by selling the ProPar uniquely designed components, can control the market for replacement parts by making the components captive items which can only be purchased from Fruehauf. (Bennett 249; Mitchell 2520-21.)[12]

(c). Sales and Service Centers

127. Fruehauf has by far the largest network of sales and service facilities in the industry. It maintains approximately 100 company-

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[11] Respondent points out that Fruehauf has been marketing ProPar parts for ten years; and that sales have reached only $5 million including sales to overseas affiliates. (Rowan 1896-97; 1982.)

[12] Ohio Body supplied ProPar under-constructions with the truck trailers it sold to a major leasing company because the company was concerned that it would lose its inventory standardization on ProPar parts and would have to double-stock such components as spring hangers, axles, bearings, wheels and landing gear parts unless it continued to go standard on Fruehauf under-constructions. (Stein 349-50.) The reason for the customer's concern about inventory standardization was that the unique Fruehauf parts in its inventory were not interchangeable with the parts Ohio Body would normally have supplied. For example, while a wheel from an Ohio Body trailer would fit almost any other trailer made, it would not fit on a Fruehauf trailer nor would a wheel from a Fruehauf trailer fit on an Ohio Body trailer because of Fruehauf's unique design. (Stein 350.)

owned branches scattered throughout the various metropolitan areas of the United States. (Complaint and Answer, Para. 4; CX 641A-B; Bachman 23; Allen 190; Stein 347; Reeve 856; Reghanti 5230, 5293.)[13] The number of Fruehauf [43] branches has increased over the past ten years, and Fruehauf stresses the capabilities offered by these centers in its sales pitch to potential purchasers. (Reghanti 5423, 5425.)[14]

128. The large capital investment required limits the number of factory-owned branches which many manufacturers can afford. (Allen 190; Fontaine 3592.) For example, Fontaine's Los Angeles branch cost an estimated $400,000, exclusive of inventory. (Fontaine 3593.)

129. A primary advantage in having a large network of company-owned branches is that it increases the marketability of products including replacement parts, in the different areas of the country. (Allen 190-91; Stein 346-47; Reeve 856.) While trailer manufacturers can and do utilize independent distributors, there was testimony that these are not as effective. Manufacturers sometimes have difficulty in supervising sales efforts and in getting the independents to devote the necessary time and attention to the products. (Bachman 22; Allen 191.) Having company-owned branches also allows the trailer manufacturer to obtain the retail as well as the wholesale profit on the trailer sales. (Stein 347; Reeve 858.) [44]

130. While service facilities are used by and are important to the smaller fleets and individual truck trailer purchasers who cannot afford their own facilities (Rowan 1984-85; Reghanti 5292), large fleets also use both manufacturer-owned branch and independent service facilities for truck trailers in addition to their own facilities. (Thompson 3421; Cox 3499; Bell 3349.) Likewise, the availability of replacement parts at service centers is a consideration of large fleets in determining from whom they will purchase truck trailers (Bell 3350.).[15]

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[13] Fruehauf's branches are "full service facilities," offering new and used trailer sales, trailer repair and replacement parts sales. (Bachman 23.)

By way of numerical comparison, Great Dane has ten factory branches (Reeve 856); Strick has four factory branches (Bachman 22-23); Dorsey has two or three factory branches (Cox 3503); Heil has two factory branches (Allen 191); Ohio has no factory branches but has recently started to set up distributorships (Stein 346); and Fontaine has 11 factory branches. (RX 34D). Of course, there are many small trailer manufacturers who have none. (Fisher 1344.)

[14] The importance of after-the-sale service in truck trailers is evidenced by Fruehauf's offering a five-year warranty covering everything made by the Fruehauf Division, which warranty is the longest range one in the industry. (CX 641A-B.)

[15] Large fleets such as PIE, consider and give some weight to the existence of sales and service outlets in determining from whom to buy trailers. (Bell 3343). However, Mr. Cox of Saunders, a full-service leasing company with 106 locations scattered throughout the Eastern United States (3453), testified that the number of service centers possessed by a trailer manufacturer is not particularly important to his company, since it maintains its own equipment (3457).

131. Respondent maintains that there is no record evidence to support the conclusion that possession of factory-owned or franchised sales and service centers are a necessary condition to entry into the truck trailer market. Respondent points to testimony that trailer maintenance is quite simple (Bachman 106), and that the minimum maintenance which is required can be done by a high school trained mechanic with hand tools. (Flagan 5076-77.) It points to additional testimony that trailers require very little maintenance work, much less than power units (Rowan 2010; Flagan 5074-75); that trailers are intentionally designed to require as little service as possible (Flagan 5074-75); and that in recent times, vehicles, components systems, and maintenance procedures have all improved. (Bell 3301.) [45] Nevertheless, it is clear from the record that trailers do require service or repair from time to time and that facilities exist for that purpose.[16]

(d). Trade-Ins

132. Sales of new trailers generally involve trading in a used trailer to the seller. (Bachman 39-40; Allen 227-28.) The ability of a truck trailer manufacturer to accept trade-ins is very important and sometimes critical in making sales. (Bachman 164-65; Allen 192-93; Reeve 868; White 4026.) The reason that many trailer customers prefer to trade in used trailers rather than dispose of the units themselves is that they are not in the used trailer business. (Allen 194; Alderson 5920.) Thus, truck trailer purchasers look for trailer manufacturers who accept trade-ins in making their purchases. (Bell 3353.)

133. It is important to a trailer manufacturer to have numerous used trailer outlets. (Bachman 38-39.) It is important for a trailer manufacturer to turn over his trade-ins or used trailer inventory because his profit from the sale of new trailers may be tied up in the traded units. (Allen 192-93.) One witness felt that by having a large number of used trailer outlets, the manufacturer is able to spread his used trailers over a series of locations in the area where the particular size and type of [46] used trailer is in demand and thus avoid having them in inventory an excessive amount of time. (Bachman 38-40.)[16a]

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[16] The trend is for large fleets to have their own service centers which perform trailer maintenance and repair work. (Bachman 23; Bell 3301; Pfund 3378; Thompson 3422, 3428-29; Cox 3480-81; Kortenhaus 3513-16.) Many of these centers are capable of complete trailer assembly. (Bell 3306, 3307; Thompson 3430; Cox 3477-78, 3481-82.) While such fact may tend to diminish the significance of the manufacturer's servicing operations, it does not affect the *sales* factor, both as to trailers and replacement parts.

[16a] The ability of a truck trailer manufacturer to take trades of used trailers at a number of different geographic locations is an important factor in selling new trailers since the point at which fleets drop off used trailers is

(Continued)

134. Fruehauf has more used trailer outlets than any other trailer manufacturer. Fruehauf accepts trade-ins and sells used trailers at all or most of its approximately 100 factory branches. (Bachman 39; Allen 193.)

135. Fruehauf's ability to handle trade-ins gives it an advantage over smaller truck trailer manufacturers who lack the ability to do so to the same extent. (Bachman 164-65.) Although small trailer manufacturers do accept trades (Reeve 868; Allen 192; Cox 3472; Alderson 5931-32), many are limited in their ability to accept trade-ins due to their limited number and location of used trailer sales facilities. (Allen 194.) Many trailer manufacturers are also limited because they cannot afford the capital costs of maintaining a large inventory of used trailers. (Allen 193.)[17] [47]

136. As respondent points out, it is possible to dispose of used trailers in other ways besides trading. (Alderson 5934.) Some fleets have no trade-ins at all; their used units are scrapped (Pfund 3386), sold directly by the fleet for transportation or storage purposes (Thompson 3424-25; Kortenhaus 3517-18) or rebuilt and refurbished by the fleet. (Thompson 3423-24.) There are also independent companies which specialize in selling used trailers. (Bell 3363-64.) Sometimes fleets can get better prices for used trailers by not trading in to manufacturers. (Kortenhaus 3517-18; Pierce 3666-68.)[18]

137. However, despite the existence of such alternative means of disposal, the fact remains that trade-ins are a fact of life in the merchandising of truck trailers. Fruehauf, with its 100 branches and financial resources, is in a better position in this regard than its competitors.

(e). Finance

138. The record contains much testimony and evidence regarding the financing of truck trailer purchases. And while, as respondent points out, alternative means of financing exist and are becoming increasingly significant, the ability of a manufacturer such as Fruehauf (and some others) to finance sales through its own captive corporate finance company remains an important and advantageous competitive factor. [48]

139. In the early and mid-1950's, users of trailers had difficulty

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important to the fleet's balance. (Bell 3353, 3364.) A trailer manufacturer that does not have a used trailer facility in the area where it accepts the trade-ins must pay the cost of transporting the traded units to its used trailer facilities for sale. (Allen 194.)

[17] There was no testimony that Fruehauf offers better trade-in terms than other manufacturers. In fact, there was testimony that Fruehauf does not do so. (Cox 3472; Bell 3362.)

[18] Mr. Cox of Saunders, a major fleet, which has traditionally traded in used units, testified that his company is looking very strongly at retailing its used trailers, as it does with tractors. (Cox 3471-72.)

in securing financing for the purchase of revenue-producing equipment (trucks, tractors, and trailers). (Gilliland 5499-5500; White 3962.) This was because of the uncertain condition of the trucking industry (of which the trailer industry is derivative), which was fragmented and unsophisticated; contained many small companies; was not very well capitalized; and had no publicly held companies. (Gilliland 5499, 5508; Pierce 3613.) Banks and other financial institutions simply did not believe that the motor carrier industry was creditworthy. Accordingly, vendor loans became virtually the only practical source of credit available. (Gilliland 5499-5500; White 3945, 3962, 3988.)

140. Fruehauf Finance was founded in 1948 to provide a source of capital for trailer purchasers, as an adjunct to the sales arm of the company. (Gilliland 5498-99; Reghanti 5287.) In 1955, 65 percent-75 percent of the company's trailer sales in dollars were financed by Fruehauf Finance. (Gilliland 5504-05, 5581.) In 1972, this figure amounted to 55 percent of all sales and leases. (44 percent and 11 percent, respectively.) (CX 756D.)

141. Besides Fruehauf, only a handful of the leading trailer manufacturers have or have had captive finance companies, *viz.*, Trailmobile, Strick, Gindy, Great Dane and Brown. (Bachman 24, 37; Allen 195; Bennett 253; Reeve 854; Gilliland 5566.)

142. Subsequent to the mid-1950's banks have grown increasingly active in truck trailer financing. But, as complaint counsel point out, banks are generally willing to finance only the most creditworthy purchasers because of the banks' higher credit standards and lack of ability to handle repossessions. (Bachman 159, 165; Reeve 902-03; Pierce 3680-82; White 4028-29.) Consequently, the major banks making loans to the transportation industry, such as First National Bank of Boston and Chase Manhatten, [49] while handling large transactions, deal only with a relatively few large purchasers. (Pierce 3674, 3680, 3682-83; White 4004-07.)

143. Apart from such specialized loan transactions involving the transportation sections of certain major banks and large trailer purchasers, other bank financing is sometimes available to smaller "non-bankable" purchasers.[19] Other departments of such banks or local branches may lend to smaller customers. (Pierce 3686-87; White 3964-68.) And there are smaller local banks which make loans for trailer purchases, sometimes through chattel mortgage or installment loan transactions, sometimes through arrangements made by trailer manufacturers who may and do guarantee the loan.

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[19] The term "bankable" refers to the ability to borrow from a major bank through its transportation sections. (Gilliland 5506-07.)

(Gilliland 5510-14, 5516, 5531-32; Pierce 3621; Goedhart 3777-79; See also Cox 3465; Allen 194-95; Stein 347; Goedhart 3766.)[20]

144. Yet, despite the existence of alternative means of financing trailer sales, financing through captive finance companies remains of significant importance. (Reeve 876-77; Goedhart 3772-73; see Bennett 254, 275-77; Bachman 99.) This is especially true as regards sales to smaller or less creditworthy customers who may have difficulty or be unable to obtain credit elsewhere. (Bachman 164-65; Allen 195-96; Reeve 854, 877.) And often large customers, such as fleets, utilize captive finance companies on occasions [50] when banks deem a purchase transaction too risky, or when a borrower has exhausted his bank line of credit, or when money is tight or limited at banks. (Bachman 35-36; Rowan 2008; tr. 5594-95, 5568-74 *in camera.*)[21]

145. In short, the record makes it abundantly clear that trailer manufacturers such as Fruehauf, which have a captive finance capability, can more effectively compete for trailer sales.[22]

C. *Exit and Entry*

146. Although there has been some entry into the truck trailer market, the record shows that at least since 1955 no entrant penetrated to become one of the top eight firms. (RX 266.) Recent new entrants include some firms as Monon, Stainless Tank & Equipment, Polar and Bertolini. (Bachman 40-41; Allen 175, 210.) Although Monon had obtained about [51] 1 percent of the market by 1973, industry witnesses looked upon the new entrants as specialized manufacturers not in the same class with those producing a wider variety of products. (Bachman 41-44; Allen 175-76, 207; Reeve 865; Reghanti 5265-66.)

147. Two major truck trailer manufacturers, Brown and Highway, exited the market since 1969. (Bachman 20; Stein 335-36; Reeve 866; Davis 1451; Cox 3490, 3496; Kortenhaus 3536; Fontaine 3594; Flagan 5135-36; Reghanti 5260-62; Alderson 5943.)

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[20] Finance companies not affiliated with trailer manufacturers sometimes finance trailer sales. These include General Electric Credit Corporation, CIT Corporation, General Motors Acceptance Corporation and Associates Finance. (Bennett 276; Goedhart 3776.)

[21] But whatever the terms of bank financing may be in comparison to Fruehauf, for the large numbers of trailer purchasers to whom the banks will not make any terms available, the point seems irrelevant.

[22] Fruehauf Financing Company also has a Transport Investment Division which makes loans to companies in the transportation industry for operating capital, expansion and other business needs. (Rowan 1944; Gilliland 5605.) Fruehauf Finance Corporation also has a subsidiary Transport Acceptance Corporation which finances the purchase of any product by transportation industry firms. (Gilliland 5563-64; CX 6602-6.) However, I do not believe it necessary to discuss these aspects of Fruehauf Finance's operations in order to reach my conclusions regarding the role of Fruehauf Finance as a valuable sales aid to respondent.

D. *Profitability*

148. Fruehauf's average return on investment on its trailer sales from 1968 to the time of trial was slightly lower than the average of all manufacturing for approximately the same period of time. (Nelson 6652, *in camera.*) Both respondent and complaint counsel agree that Fruehauf's profitability serves as a reasonable proxy for the trailer industry as a whole because they have a large share of the market. (Nelson 6650.)

149. Profitability figures were used by both economists to test previously arrived at conclusions about the industry as opposed to inferring anything about the industry solely from the data. (Mann 5730-31.) It was recognized by both parties that even though high profitability evidences high barriers, low profitability does not necessarily mean low barriers because excess profits may be consumed by inefficiencies. (Nelson 6621.)

150. Given the inexactitude (see Mann 5726) of the calculations of profitability for a firm or an industry, and that estimates for Fruehauf are not extreme either on the high or low side, the figures favored by both respondent and complaint counsel must be viewed as indeterminative. [52]

VII. HEAVY DUTY WHEEL MARKET

151. As for wheels, the complaint alleges the existence of one relevant market and two submarkets. (Complaint ¶ 12.):

(a) Manufacture and sale of heavy duty wheels; and

(b) Manufacture and sale of truck trailer wheels;

(c) Manufacture and sale of cast spoke truck trailer wheels, exclusive of rims;

152. For the reasons set forth at the commencement of my Legal Discussion, *infra* at VIII, I have concluded that only the overall heavy duty wheel market is the appropriate wheel market (on this record) for examination of Section 7 effects.

A. *Market Structure*

153. A heavy duty wheel consists of a hub, a center member (with a non-demountable rim in the instance of a disc wheel) and a brake drum. (Allen 179; Reeve 858-59; Smith 914; Mitchell 2507-08.)

154. Most heavy duty wheels are designed for application on axles with a rated gross vehicle weight ("GVW") capacity of 19,500 pounds and above. (Rupert 776; Reeve 863; Zart 1218, 1220; Fisher 1333; Fairchild 1624; Kenney 2079; Krauss 2354.)

155. There are basically two types of heavy duty wheels, *viz.*, cast

spoke and disc, which are not freely interchangeable on the same vehicle and are generally not found in the same fleet. (CC's 1st RACF - #1; Bachman 46; Allen 179; Rupert 798-99, 802, 833; Reeve 858-59.) Cast spoke and disc wheels [53] are both useable on a given size axle, but are not mixed on the same axle. (Rupert 798.) Trucks sometimes have both types mounted on the same vehicle. (Zarella 5960.)

156. A cast spoke wheel consists of a center member called a "spider," with an integral hub, brake drum and demountable rim. (RX 200; Reeve 858; Mitchell 2507-08.) (See depiction in RX 112.)

157. The spider and drum are usually sold assembled together with the bearing cups, rim clamps, studs and spacer bands. (CX 35N-O; CX 52A; CX 49F; Rupert 769, 772, 777, 798-99; Reeve 859; Smith 914; Looney 1807; MacDonnell 2019; Vause 2239; Mitchell 2507-08.) However, some customers such as Mack Truck and International Harvester purchase some of their cast spoke spiders and drums separately and assemble them. (R's 2nd RAF - #33; Vause 2227; Mitchell 2567.) Rims are usually purchased separately and attached to the wheel and drum assembly by the OEM. (Rupert 772, 799; Smith 914; Kenney 2082; Mitchell 2508.) Rims account for approximately 10 percent of the cost of a heavy duty cast spoke wheel. (Mitchell 2526.)

158. A disc wheel consists of a hub, brake drum, disc, and rim which has been permanently attached to the disc, plus various minor parts. (RX 205; Reeve 859; Smith 914; Zart 1233, 1237; Kenney 2083, 2095, 2099; Vause 2184.) The hub of a disc wheel is similar to the integral hub of a cast spoke wheel but is smaller. (Reeve 859.) (See depiction in RX 109.)

159. The user of a disc wheel usually buys a hub and drum assembly and mounts it to a disc with its integral rim. (Rupert 799; Reeve 859; Fairchild 1634; tr. 2099, 2161-62 *in camera;* Krauss 2365-66; Mitchell 2508.) Frequently heavy duty axles are sold with attached hubs and drums when disc wheels are to be used. (Fisher 1342; Davis 1409, 1419; Phillips 1569, 1574.) A heavy duty cast spoke wheel with two rims performs the same basic function as two heavy duty disc wheels and a hub. (R's 1st RAF - #34.) [54]

160. Drum and hub assemblies account for approximately 50 percent of the price of a heavy duty disc wheel. (Krauss 2366.)

161. Heavy duty cast spoke and disc wheels compete for direct sales to vehicle producers and indirect sales to the ultimate users. (RX 130; RX 135A-B; RX 136A-B; RX 137; RX 152A-B; Rupert 825-26; Kenney 2144; Krauss 2385-86.)

162. Imports of heavy duty wheels and their components have been insignificant. (Rupert 794; Smith 930; Zart 1233-34, 1242;

Fisher 1347; Krauss 2422–23; Mitchell 2515.) Imported cast spoke wheels and hubs are more expensive than those produced domestically. (Davis 1422; Mitchell 2515.) To adapt Japanese heavy duty wheels for use on domestic vehicles would require extensive changes. (Zarella 5965.)

163. While the complaint's definition of "wheels" has an inherent logic in that it encompasses all components connecting the tire and the axle (Bachman 75; Reeve 879), it should be noted that components of a wheel assembly may well be supplied by different companies. For example, disc wheel supplier Firestone, does not make hubs and drums. (Zart 1236.) Rockwell only makes hubs and drums (CC's 1st RAF - #18); some manufacturers of demountable rims for use with a cast wheel — Firestone, Motor Wheel Division of Goodyear (hereinafter "Motor Wheel") and Redco — do not make cast wheels. (Rupert 772–73, 829.) And several OEMs, such as International Harvester, Mack and Utility, purchase all heavy duty wheel components separately. (Mitchell 2567; Vause 2226–27; Zarella 5969–70; Bennett 294, 323.)

164. There are seven significant producers of the spider or disc components of finished heavy duty wheels, *viz.*, Dayton-Walther Corporation (hereinafter "DW"), Gunite Division of Kelsey-Hayes (hereinafter "Gunite" or "Kelsey-Hayes"), Webb Wheel Division of [55] Marmon Industries (hereinafter "Webb"), Erie Malleable Iron Company (hereinafter "Erie"), Firestone Tire & Rubber Company (hereinafter "Firestone"), The Budd Company (hereinafter "Budd"), and Motor Wheel. (CX 569; Rupert 768; Smith 913; Zart 1187, 1235; MacDonnell 2014; Kenney 2079, 2096; Vause 2189; Mitchell 2498, 2514.) In addition, Alcoa produces only aluminum disc wheels, the sales of which have been insignificant due to their relatively higher cost. (Bachman 50; Rupert 844; Smith 929; Rowan 1924–25; Kenney 2096; Krauss 2367; Mitchell 2514.)[23]

165. The major sellers of heavy duty wheels generally produce either the spider for the cast spoke wheel or the disc for the disc wheel. (CC's 1st RACF - #5, 8, and 14; Rupert 768, 798; Smith 929; Looney 1802; MacDonnell 2032; Vause 2185, 2189; Krauss 2374–75; Mitchell 2514.) Each of the spider producers also manufacture heavy duty drums and all but the smallest, Erie, also make hubs. (CX 35A–T; CX 49A–X; CX 50A–P; Rupert 768; Smith 913, 921; MacDonnell 2014; Vause 2181–82; Mitchell 2499.)

166. There are certain common elements in the manufacture of

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[23] Aluminum disc wheels represent a small percentage of the market. (Zart 1237; Krauss 2367.) They are lighter than cast spoke wheels but are much more expensive. (Zart 1243; McGroarty 3696.) Firestone's sales of aluminum discs are insignificant compared to its sales of steel discs. (Zart 1237.)

various heavy duty wheel components. Spiders for cast spoke wheels, drums and nonintegral hubs are produced by the same major competitors. (See previous finding.) These components can be and are machined (finished) in the same plant using the same equipment with modified tooling. (Smith 959-60, 983; Fisher 1316; Mitchell 2525.) Castings for nonintegral steel hubs and spiders can be produced in the same foundry. (Mitchell 2529.) [56]

167. In like manner, the disc producers, except for Alcoa, also manufacture rims. (CX 23A-D; 37Z-87; 39A-L; Rupert 773, 829; Zart 1186-87, 1230; MacDonnell 2020; Kenney 2079; Krauss 2353; Mitchell 2516, Vause 2184-85.) Three of the five disc producers make heavy duty drums and hubs. (CC's 1st RACF - #8, 18, 25, 28, 29; CX 40P; CX 41A-Z-19; CX 48A-Z-11; CX 54A-D; CX 67F; Fisher 1346-47, 1357; MacDonnel 2014, 2019, 2031; Kenney 2079, 2094-97; Vause 2181-82; Krauss 2352, 2375-76.)

168. There are four producers of cast spoke wheel spiders, *viz.*, DW, Gunite, Webb, and Erie. (CC's 1st RAF - #8; CX 35A-T; CX 49A-X; CX 50A-P; Rupert 768, 798; Smith 913, 926-27; MacDonnell 2014, 2032; Vause 2181-82, 2189; Krauss 2375; Mitchell 2507, 2514, 2522; see Looney 1802; Zarella 5954.)

169. There are 5 producers of the principal component of the heavy duty disc wheel, the disc. These firms are: Firestone, Budd, Motor Wheel, Kelsey-Hayes and Alcoa. (CC's 1st RAF - #5; CC's 1st RACF - #22, 23; CX 24A-D; CX 27A-Z-19; CX 40A-P; Rupert 798, 823; Smith 929; Zart 1187, 1235, 1239-40; MacDonnell 2016-17, 2032; Kenney 2079-80, 2096; Vause 2181-82, 2184-85, 2189; Krauss 2352, 2374-75; Mitchell 2514; McGroarty 3740; Zarella 5955.) Three firms, Firestone, Motor Wheel and Budd, dominate the production of discs. (Zart 1239-40; Kenney 2096; Krauss 2374.)

170. It was estimated that imports, chiefly of SKF and Michelin, were less than one percent of heavy duty disc wheel sales in 1974. (Zart 1242; Krauss 2422.)

171. Kelsey-Hayes produces discs for the lighter end of the market, namely 14,000-26,000 GVW. (CX 560B; MacDonnell 2016-17; Kenney 2096; Vause 2181, 2185-87.) [57]

172. Motor Rim and Wheel, Standard Rim and Wheel, Wisconsin Rim and Wheel, Southeast Rim and Wheel, Southwest Rim and Wheel, H&H Wheel Service and Oakland Wheel and Rim make disc wheels for specialty applications, do not make their own rims and accounted for less than 5 percent of the disc wheel production for all uses in 1972. (Zart 1240-41; Krauss 2421-22.) These firms produce only specialty wheels for different applications than those made by Firestone, Budd or Motor Wheel. (Zart 1241-42; Krauss 2421-22.)

173. Three of the axle producers make both heavy duty hubs and drums which are often sold attached to their axles. (CX 37Z-88; CX 92-93; Davis 1409; Fisher 1316, 1346-47; Phillips 1569.)

174. Drums used as part of heavy duty cast spoke and disc wheels are substantially the same except for machining. (Jones 1282; Fisher 1378-79; Looney 1828; Kenney 2084, 2164-66; Mitchell 2526, 2566.) The producers of heavy duty drums sometimes sell them for use as part of both cast spoke and disc wheels. (Fisher 1379; Fairchild 1650; Looney 1828.)

175. The following companies are producers of finished drums for use as part of heavy duty wheels: DW, Gunite, Webb, Rockwell, Erie, Budd, Motor Wheel, Durametal, Reyco, Standard Forge, Truck Brake Service (Ful-Rib), Kershaw (Dana), General Foundry, International Harvester Corporation (hereinafter "IHC"), and Utility Trailer Company (hereinafter "Utility"). (CC's 1st RAF - #8, 18, 25, 28, 29; CX 35A-T; CX 37Z-51-84; CX 40A-P; CX 41A-Z-19; CX 48A-Z-10; CX 51A-D; CX 54A-D; CX 67F; RX 56A-L; Bennett 289-90; Rupert 768; Smith 913, 987-88; Fisher 1315, 1346-47; Davis 1407, 1420; Phillips 1569; Fairchild 1623, 1629, 1637; Looney 1793, 1805; McCorry 1835-36, 1841; MacDonnell 2014, 2019, 2031; Kenney 2079, 2094-95; Vause 2181-82; Krauss 2352, 2375-76, 2409; Mitchell 2498, 2508, 2516, 2524.) [58]

176. Of these producers of finished heavy duty drums, six make the spider or disc portion of the heavy duty wheel. These six include all but one of the significant producers of heavy duty wheel spiders or discs. As discussed below, of the remaining heavy duty drum suppliers who do not produce spiders or discs, three, Rockwell, Standard Forge and Kershaw, produce hubs and sell axles with attached hubs and drums, two are vehicle producers, IHC and Utility, manufacturing for in-house use only, and three are *de minimis* factors in the market, Truck Brake Service, General Foundry and Durametal. (Findings CX 37Z-87-88; Davis 1410.)

177. Of the heavy duty drum producers, Motor Wheel, Webb, Rockwell, Reyco, Kelsey-Hayes and DW offer an extensive product line. (CX 37Z-46-85; CX 41A-Z-19; CX 48A-Z-10; CX 50A-P; CX 51A-D; CX 54A-D; CX 527A-Z-31; Fisher 1342, 1345; Looney 1823-24.)

178. IHC makes roughly 30 percent-50 percent of its own heavy duty drums, but does not sell finished drums to other manufacturers. (Looney 1805; Kenney 2095; Vause 2227, 2238-39; Krauss 2409, 2423-24; Mitchell 2516.)

179. Truck Brake Service (Ful-Rib) sells to the aftermarket with very limited production. (Smith 987-88, 996-97; Fairchild 1637.) It

does not have the necessary foundry to cast brake drums and has sold some of its machining equipment to Durametal in return for drum castings. (Fairchild 1641-43.)

180. Only 1 percent of General Foundry's drum product sales are finished drums, and these are finished by subcontractors. General Foundry has restricted its activities in finished heavy duty drums because of the cost of maintaining the necessary inventory of finished drums and because of its noncompetitive prices. (McCorry 1836-38, 1841.) General Foundry does not make a full line of finished drums but offers only two or three part numbers today. (McCorry 1846.) [59]

181. Durametal sells 60 percent of its brake drums to the aftermarket and partially attributes its market survival to its insulated position in the Pacific Northwest. (Fairchild 1652, 1656.) However, although Durametal's prices are competitive in some cases, Durametal's price is 15 percent-20 percent higher than that of Gunite on drums sold to Paccar. (Fairchild 1638.) Durametal markets primarily in 11 western states due to freight costs. (Davis 1416, 1448-49; Fairchild 1633-34.)

182. J&J Casting does not presently produce heavy duty drums. (Jones 1267.) J&J Casting began production of heavy duty drums in 1970 and ceased production in 1973. It sold to the aftermarket on a very limited basis. (CX 563; see also CX 564A-D; Jones 1267, 1274-75.) Its heavy duty drums were more expensive than other heavy duty drums sold to vehicle producers. (Jones 1276.)

183. The following companies are producers of the hub component for use as part of a heavy duty wheel, specifically the heavy duty disc wheel: Rockwell, Budd, Motor Wheel, Paccar, Mack, DW, Webb, Kelsey-Hayes, Kershaw, Utility, Standard Forge, Conmetco and Kaiser Aluminum. (CC's 1st RAF - #18, 28, 29; Bennett 288; Smith 913; Fisher 1315, 1346, 1357; Davis 1407, 1409, 1420; Phillips 1563; Fairchild 1649, 1653; MacDonnell 2019, 2031; Kenney 2079, 2097; Vause 2182; Krauss 2352, 2409; Mitchell 2498, 2508, 2529; McGroarty 3738; Zarella 5955-56.)

184. Imports of heavy duty hubs are very rare and involve prohibitive costs and long delivery times. (Fisher 1347; Davis 1422; Krauss 2374.)

185. Of the above hub producers five produce the spider or disc components of a heavy duty wheel, four others produce heavy duty drums, three, Paccar, Mack and Conmetco, are vehicle producers making for [60] in-house use only, and the remaining firm, Kaiser,

has only a single customer. (Fisher 1347; Davis 1407; Fairchild 1635; Kenney 2097; Krauss 2409, 2424; Zarella 5955-56, 5969.)[24]

186. Hubs can be cast of aluminum, malleable iron, cast iron or steel and can be forged of aluminum, malleable iron or steel. (Smith 917, 959; Fairchild 1634, 1653; tr. 2154-56 *in camera;* Krauss 2364; tr. 2412 *in camera;* Mitchell 2527; McGroarty 3746; Zarella 5956.)

187. Each type of hub has specific applications and uses. (tr. 2158-59 *in camera;* Krauss 2364; Zarella 5956.) Forged aluminum hubs tend to be used in high speed, light weight applications; forged steel in relatively light weight, low cost trailer applications; and cast, malleable or ductile iron in drive axle and some steering axle applications. (Fisher 1355-56; tr. 2159 *in camera.*)

188. It is desirable for a vehicle producer to offer hubs made of steel and aluminum castings and forgings so as to meet various customer preferences. (Tr. 2158 *in camera;* Krauss 2364.) For a given hub, the choice of material or process is dictated by the costs or feasibility of its production. (Krauss 2364; Mitchell 2528.)

189. Many of the hub producers buy the castings or forgings which they then machine. (Fisher 1367-72; Davis 1408; Phillips 1567; Kenney 2097; tr. 2154-56 *in camera;* Krauss 2357; Mitchell 2528; Zarella 5955-56.) [61]

190. There is specialization by the producers of the unfinished hubs according to each of the manufacturing processes and materials. (Fisher 1370; tr. 2157-58 *in camera.*) Generally, suppliers of castings do not make forgings and suppliers of forgings do not make castings. (Fisher 1336, 1365-66; tr. 2157-58 *in camera;* Krauss 2364-65.)

191. Producers of the rim component for use as part of a heavy duty wheel include Firestone, Motor Wheel, Budd, Redco and Kelsey-Hayes to a limited extent.[25] (CX 23A-D; CX 30A-B; CX 31A-C; CX 39A-L; Rupert 772-73, 829; Smith 929; Zart 1186-87, 1230; Sechrist 1865, 1873, 1880; MacDonnell 2020; Kenney 2079; Krauss 2353; 2376; Mitchell 2516.)

192. Heavy duty rims can be used as part of either cast spoke or disc wheels, and production shifts between making rims for cast spoke and disc wheels can be accomplished with little or no difficulty. (Zart 1232-33, 1259; Sechrist 1877; Kenney 2081-83; tr. 2120 *in camera.*)

193. Firestone, Motor Wheel and Budd are the leading producers of heavy duty rims. Firestone and Motor Wheel have the most

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[24] Kaiser's only sales of finished components for heavy duty wheels are of hubs that it sells to a single customer, Paccar. (Kenney 2097; McGroarty 3738.)

[25] Imports of rims are few. Some were imported at a considerable price premium during the 1974 strike. These accounted for less than 5 percent of the market. Such importation has virtually ceased. (Zart 1233-34.)

complete lines of rims and Budd offers the most popular sized rims. (CX 23A-D; CX 27T-Z-4; CX 39A-L; Zart 1231.) These [62] three are considerably larger than Redco which makes only five part numbers of demountable rims which are sold for use as part of cast spoke wheels for trailers. (Sechrist 1865, 1880; see CX 30A-B; CX 31A-D; Zart 1231.)

194. Kelsey-Hayes makes rims for medium GVW truck disc wheels at its Romulus, Michigan plant. (Zart 1231-32, 1251; MacDonnell 2020.)

195. Table One summarizes the market structure of heavy duty wheels in terms of components sold. Table Two summarizes market shares.

TABLE ONE

HEAVY DUTY WHEEL COMPONENTS SOLD BY EACH MANUFACTURER

Firm	*Spider*	*Disc*	*Hub*	*Drum*	*Rim*
Firestone		X			X
Dayton-Walther	X		X	X	
Kelsey-Hayes	X	X	X	X	X
Budd Co.		X	X	X	X
Motor Wheel		X	X	X	X
Rockwell			X	X	
Webb	X		X	X	
Reyco				X	
Alcoa		X			X
Redco					
Erie	X			X	
Standard Forge			X	X	
Truck Brake Service				X	
Durametal				X	
General Foundry				X	
Kershaw			X	X	
Kaiser			X		
IHC				X	
Utility			X	X	
Paccar			X		
Mack			X		
Conmetco			X		

TABLE TWO

Heavy Duty Wheels Market Shares 1970-1972

(000's)

	Firm	Source Admission Paragraph No.	1970		1971		1972	
				%	$	%	$	%
	Firestone	(38, 39, 40[1])						
	Dayton-Walther	(41, 42, 43[2])						
	Kelsey-Hayes	(44, 45, 46[2])						
Top Four	Budd Co.	(50, 51, 52[3])	132,192	70.71	125,640	65.43	154,922	69.52
	Motor Wheel	(53, 54, 55[4])						
	Rockwell	(56, 57, 58[2])						
	Webb	(CX 513, Smith 921)						
Top Eight	Reyco	(65, 66, 67[2])	177,316	94.86	179,241	93.06	223,035	93.05
	Alcoa	(59, 60, 61[5])						
	Redco	(68, 69, 70[2])						
	Erie	(62, 63, 64[2])						
	Standard Forge	(71, 72, 73[2])						
	Truck Brake Service	(80, 81, 82[5])						
	Durametal	(77, 78, 79[2])						
	General Foundry	(89, 90, 91[5])						
	Southwest Wheel	(86, 87, 88[2])						
	Kershaw	(83, 84, 85[2])						
	Hutchins	(92, 93, 94[5])						
	J&J Casting	(95, 96, 97[5])						
	Kaiser	(74, 75, 76[5])						
		Totals	186,919	99.98	192,607	99.99	239,655	99.99

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[1] Complaint Counsel's Second Request for Admissions of Confidential Facts and Response Thereto, as modified at Tr. 1247-49 (Mr. Zart testified that the figure stipulated to by Counsel erroneously included sales totalling $6.3 million in 1972).

[2] Complaint Counsel's Second Request for Admissions of Confidential Facts and Response Thereto.

[3] Complaint Counsel's Second Request for Admissions of Confidential Facts and Second Supplemental Response Thereto.

[4] Complaint Counsel's Second Request for Admissions of Confidential Facts and Response Thereto, as modified at Tr. 2174 (Mr. Kinney testified that the figure stipulated to by Counsel erroneously included sales totalling $10 million in 1972).

[5] Complaint Counsel's Second Request for Admissions of Confidential Facts and First Supplemental Response Thereto.

196. The customers for cast spoke wheels tend largely to be different from those of disc wheels. Members of the trucking industry, operating primarily in the west, and particularly those operating on the West Coast, tend to use disc wheels, while customers east of the Mississippi River tend to use cast spoke wheels. (Bachman 51, 133; Stein 339; Rupert 843; Smith 915.)

197. Generally, fleets do not have both cast spoke wheels and disc wheels in their fleets at the same time, due in part to their desire to simplify their maintenance procedures. (Smith 915.) In ordering new equipment, fleets usually specify either the cast spoke wheel or disc wheel. (Bachman 51; Stein 354; Reeve 860.) For example, fleets like Roadway, PIE, and UPS use disc wheels, while other fleets like North American, and Yellow Freight specify only cast spoke wheels. (Bell 3329, 3336; Pfund 3392; Thompson 3439; Kortenhaus 3521-22; Alderson 5919.)

198. However, there is no question that both heavy duty cast and disc wheels are sold to the same *class* of customers. (R's 1st RAF - #12; Nelson 7098.) Both types of wheels have been and [65] are purchased by the same truck, truck tractor and truck trailer OEMs

and the same types of end-users. (RX 267Z–8.) And both types of wheels are used on trucks, truck tractors and truck trailers. (R's 1st RAF - #9 & #10.)

199. Heavy duty disc and cast wheels have identical channels of distribution. (McGrath 4855; RX 267Z–4, Z–8, Z–33.) Both are handled in the aftermarket by the same types of distributors and outlets. (R's 1st RAF - #14.)

200. Disc and cast wheel manufacturers actively compete. (Nelson 7098.) This competition is reflected in their respective marketing and sales efforts, their advertising, and their technological and design efforts. In recent years, Budd, Motor Wheel and Firestone, the disc wheel producers, have concentrated much of their marketing effort on OEMs and fleets that are or were standard on cast wheels. (Krauss 2385; Kenney 2144; Rupert 823.) Cast wheel producers are responding with advertising (Mitchell 2559–65), marketing and technical efforts. (Smith 963; Mitchell 2530, 2570.)

201. The disc manufacturers' marketing efforts directed at cast customers have included contacts by their field sales people of fleets, sales presentations to major OEMs (as exemplified by RX 143, Budd's presentation to Mack Truck) and extensive testing to compare the performance characteristics of disc and cast wheels to gain data for their sales efforts. (RX 143; Krauss 2385, 2394.)[26] [66]

202. The advertising of major disc and cast producers in recent years likewise demonstrates the head-to-head nature of competition. Budd's ads, for example, compare cast wheels and Budd disc wheels in terms of fuel savings (RX 130, RX 137, RX 152 A&B), less maintenance (RX 130, RX 135 A&B, RX 136 A&B, RX 137, RX 152 A&B; Krauss 2389), improved tire mileage (RX 137, RX 152 A&B), and better driver comfort (RX 136 A&B, RX 137). On the other hand, much of Dayton-Walther's advertising emphasizes the alleged advantages of cast over disc wheels in terms of weight savings (Mitchell 2559–60, 2562; CX 574C, CX 575C, CX 610), cooler running (Mitchell 2561–63; CX 574J, CX 571, CX 610), and tire life (Mitchell 2562, 2564–65; CX 569, CX 575). According to Mr. Mitchell, the objective of Dayton's advertisements are principally to obtain specifications for cast wheels and particularly for Dayton wheels. (Mitchell 2564.)[27] [67]

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[26] The seriousness of these marketing efforts was demonstrated by the unwillingness of an official of Dayton-Walther, a cast wheel producer, to identify on the record fleets that have switched from disc to cast because "[t]he disc people would go back to see them again." (Mitchell 2431.)

[27] Competition between disc and cast is reflected in technological and design efforts. Webb Wheel designed and developed the three-spoke cast wheel as "a marriage between a disc and a spoke wheel" in an attempt to overcome performance and safety problems with the traditional cast wheel that Budd had exploited in the West. (Smith 963.) Dayton-Walther "intend[s] to do something" about recent disc penetration (Mitchell 2530), which would include efforts of both a technical and marketing nature. (Mitchell 2570.) Disc wheel producers, on the other hand, have

(Continued)

203. Alleged advantages of cast over disc include:

a. cheaper (Bachman 50; Allen 181; Rupert 800, 802; Reeve 859; Smith 915; Zart 1243; Kenney 2177; Krauss 2429; Mitchell 2518; see also CX 575B–C);

b. lighter (Rupert 800; Smith 915–16; Krauss 2429);

c. stronger (Rupert 800; Mitchell 2518);

d. easier to change the tires (Rupert 800–01; Smith 914–16);

e. run cooler, thus giving better brake and tire life (CX 237U, CX 571, CX 574J; Mitchell 2518, 2561, 2563);

f. last longer (Cox 3497);

g. cheaper to run (Smith 916; Cox 3497); and,

h. easier stocking for replacement in the field (Alderson 5919).

204. Alleged advantages of disc over cast include:

a. easier to keep aligned (Kenney 2144; Krauss 2389; Mitchell 2519; see Rupert 825–26; Smith 916; but see CX 570);

b. able to use an outboard mounted drum (Kenney 2145; Krauss 2404);

c. easier to change wheel sizes (Krauss 2404), and,

d. have a potential for weight savings (Kenney 2144). [68]

205. Although the initial purchase price of a cast wheel assembly may be lower than that of a comparable disc wheel (Allen 181; Smith 915; Reeve 859), there are some who believe that the use of disc wheels results in lower operating costs. If this is true, it would tend to negate an initial price disadvantage. (See McGrath 4959–61.)

206. There was much dispute in the record concerning whether recent years had evidenced a growing "trend" towards greater usage of disc wheels. Many witnesses testified to this effect (Bennett 295; Stein 354; Rupert 825; Smith 931; Fisher 1381–85; Kenney 2140; Krauss 2430; Mitchell 2529; Davis 1454; Dahl 4088–89). A market study commissioned by respondent estimated a disc usage increase from 15.6 percent in 1965 to 36.3 percent in 1974, and to 42 percent in 1975. (RX 267Z–33; McGrath 4742, *et seq.*) Actual data subpoenaed from manufacturers by complaint counsel showed an increase of only 1.9 percent over the 1968–1975 period. (CX 717A, *in camera.*) In view of my belief that the only valid wheel market on this record is the overall heavy duty wheel market, and the fact that both types of wheels are included in it, the existence and degree of any disc wheel "trend" appears to be of little or no consequence to the issues.

207. Cross-elasticity of supply between heavy duty drums and rims for use with disc and cast wheels is high. (Mann 5829.) Dr.

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developed and emphasized in their sales efforts the outboard mounted brake drum. (Krauss 2404; Kenney 2145; RX 135 A&B.) The outboard mounted drum, which cannot be used with a cast wheel, permits easier maintenance. (Krauss 2404; Kenney 2145; RX 135 A&B.)

Nelson termed cross-elasticity with respect to drums for cast and disc application as "very high or infinite." (Nelson 7090-91; Looney 1828; McCorry 1857; Jones 1282.) Likewise, rims for disc and cast wheels can be and are made on the same equipment and in the same facilities. (Krauss 2355.) [69]

208. The same manufacturing plants and facilities employed in the production of heavy duty wheels for trucks and truck tractors can be and are used for the production of wheels for truck trailers. (R's 1st RAF - #17.) Disc wheels for truck and trailers are identical. (Kenney 2145; Krauss 2406.)

209. With respect to heavy duty cast wheels, the equipment used to make truck wheels is basically the same as that used to make trailer wheels. (Mitchell 2521.) Both truck and trailer wheels can be and are run in the same foundry (Vause 2184) with only 20 minutes to an hour necessary to convert from producing truck wheel castings to castings for trailer wheels. (Rupert 809-10; Smith 965-66.) Moreover, the machining of truck drive wheels and trailer wheels is interchangeable on the same machine line. (Vause 2225.)

210. Since heavy duty cast wheels for trucks and trailers can be and are produced in the same facilities, and heavy duty disc wheels for trucks and trailers are identical, the cross-elasticity of supply between heavy duty truck and trailer wheels is "virtually infinite."

211. Three of the four cast wheel producers make both heavy duty truck and trailer wheels. (Smith 964-65; Mitchell 2521; Vause 2184.) Erie, which presently makes only trailer wheels, formerly made truck wheels but withdrew because of the "closer pricing" nature of the truck wheel business and a reluctance to be dependent on one or two customers. (Rupert 774.) There are no technological or engineering barriers to Erie's production of truck wheels. (Rupert 817-18.) [70]

B. *Barriers to Entry or to Effective Competition*

1. Capital Costs

212. There is considerable disagreement between respondent and complaint counsel as to the capital costs of entering the heavy duty wheel market. Respondent suggests costs as low as under $2 million, and complaint counsel's estimates range as high as $20 million. However, these estimates are based upon different modes of entry into the market.

213. A company could enter the market by manufacturing the spider or various other components of a heavy duty wheel, such as drums or rims, or a combination of such components. Entry into the

heavy duty wheel market could also be effected by producing disc wheels, or the drums, hubs, discs or rims attendant thereto.

214. Examining capital costs from the cast spoke standpoint, it should be observed that spiders are generally made from steel and drums from iron. Entrance into the market would probably be less expensive, as respondent points out, if the spider were also made from ductile or malleable iron.[28] However, only one firm in the industry was identified on the record as manufacturing non-steel (iron) wheels — Erie Malleable — and witness Rupert of Erie indicated that his manufacturing costs were slightly higher than Gunite's. (Rupert 779; see Mitchell 2533.) While it is true that one company with foundry capabilities, Ford, was investigating [71] the purchase of ductile wheels, it nevertheless appears that cast steel spiders are preferred over iron. (Greenberg 4685–96; Brosnahan 4546–47; see Looney 1820.)

215. Both respondent and complaint counsel cite the testimony of Mr. Joseph Greenberg, respondent's expert witness on foundries. (RX 280; RX 281; Nelson 7018–19.) Mr. Greenberg testified concerning entry into wheel manufacture at four different levels of plant addition and at various levels of production, ranging between 50,000 and 300,000 units per year. (He assumed the combined production, but in separate facilities, of both wheels and drums.)[29] His first possible entry level envisioned the use of ductile iron for wheels and cast iron for drums, and only adding some machine shop equipment to an otherwise fully capable facility. Assuming the manufacture of ductile iron wheels to be a realistic alternative, Mr. Greenberg's estimate for the cost of entry in this manner ranged between $1.6 million and $6 million. (RX 280A; Greenberg 4617–20.)

216. Mr. Greenberg's second entry level assumed the manufacture of cast steel wheels and cast iron drums and the probable addition of some foundry equipment to an existing plant. This mode of entry was estimated to range between $4.1 million and $12.7 million, depending on output levels and on whether or not new or used equipment was to be purchased. (RX 280A; Greenberg 4617–20.)

217. Mr. Greenberg's third possible entry level consisted of plant addition together with new buildings, again using cast steel for wheels and cast iron for drums. The entry was estimated by [72] Mr. Greenberg to cost between $7.4 and $18.7 million, again depending upon the choice of purchasing new or used equipment and desired output levels. (RX 280A; Greenberg 4617–20.)

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[28] Cast steel spiders and cast iron drums are generally manufactured in different foundries. (Mitchell 2526.)

[29] As noted, six of the eight manufacturers of wheel center members also make drums.

218. This foundry expert also estimated the cost of entering the industry from scratch with a new plant on a new site. For the highest level of production considered by Mr. Greenberg, 300,000 units per year, he testified that the cost with new equipment would be $20 million or, with used equipment $14.7 million.[30] Mr. Greenberg also estimated costs of $8–11 million for a plant producing 100,000 units per year. (RX 280A; Greenberg 4617–20.)

219. Mr. Greenberg went through a similar analysis for drum production alone. His estimates ranged from under $1 million to $9.2 million. (RX 280E.)

220. Other record evidence from which can be derived an estimate of capital costs for entry into heavy duty wheels is as follows:

(1) One witness estimated the cost of constructing a foundry and machine shop to produce 120,000 cast wheel spiders per year to be $8–10 million. (Bachman 58, 135.) Another witness estimated the costs for a foundry alone (to produce 240,000 wheels and drums annually), without providing for land or startup materials, to be $8–10 million. (Smith 938–39.) Costs of machining facilities, inventory and land would have to be added to obtain the total capital costs. Still another witness testified it would cost $10–20 million to open a ductile foundry, or somewhat less if the foundry were dedicated to a specific product line. (Rupert 790.) [73]

(2) For a gray iron foundry intended for the production of brake drums only, the cost estimates in the record ranged from $3–4 million (for a non-automated, high cost foundry with a semi-automated molding line) to $13 million. (Looney 1798–1801; McCorry 1840, 1861.) One witness made an estimate of $2 million for a machine shop to finish heavy duty drums, and another made an uncertain estimate of $5 million. (Fairchild 1630; Looney 1799.)

(3) Another capital cost consideration involves tooling costs for the production of the various spider patterns. Each cast spoke spider pattern costs approximately $20,000 to $25,000. (Rupert 781; Mitchell 2511, 2520.) Dayton-Walther uses about 100 different trailer wheel patterns. (Mitchell 2511.) However, additional pattern cost is often borne by the purchasing OEM. (Clem 2749–50.)

(4) In addition, there are inventory costs, estimated at about $2 million, which must be taken into account in the heavy duty wheel market. (Smith 955.)

(5) Witness Fisher from Rockwell estimated that duplication of Rockwell's hub finishing operation with new equipment would cost

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[30] The witness acknowledged that "given a choice, new equipment generally would be purchased." (Greenberg 4998.)

$8.5 million for equipment alone, and that to duplicate Rockwell's drum finishing operation with new equipment would cost $1.8 million for equipment only. (Fisher 1316-20.)

(6) Expansions and additions to existing facilities are also indicative of capital costs for entry. One company that rebuilt a foundry to cast drums and hubs spent more than $10 million. Prior to this rebuilding the foundry alone cost $10 million, bringing that firm's total capital costs for those particulars to $20 million. However, as respondent [74] points out, this foundry was unsuited for producing wheels when it was purchased and another more suitable foundry might have been purchased and rebuilt less expensively. (Tr. 1324-26 *in camera;* Greenberg 4599A-4602.)

221. Respondent's own Gunite Division completed a $25 million expansion of its heavy duty wheel facilities in 1973. (CX 6600.) This expansion increased Gunite's heavy duty wheel capacity by 50 percent and its drum capacity 100 percent. However, such expansion may well have been in excess of the minimum efficient scale. (MacDonnell 2033; CX 717B *in camera.*)

222. Costs for entrance into the heavy duty wheel market on the disc side appear to be somewhat lower than for entrance into the cast spoke market. The cost of one producer's plant which makes only rims and discs (and not a full line) was $8 million. (Tr. 2359-60; tr. 2362 *in camera.*) Another firm increased its rim and disc capacity by 30 percent by building a plant which makes a partial line of discs and rims. This construction project was budgeted for $17.5 million and something in excess of $13 million was actually spent. (Tr. 1187-88; 1204 *in camera,* 1208 *in camera,* see CX 558E *in camera.*) Still another disc wheel producer planned to expand from producing 200,000 discs per year to 600,000 per year and budgeted for a cost between $5-6 million. Its plans to expand its drum capacity by 20 percent was expected to cost $1.8 million. (Tr. 2117-18, 2148 *in camera.*) Witness Sechrist of Redco estimated it would cost about $3 million to put in a rim line. (Sechrist 1865, 1870.)

223. Based upon the above record evidence it is my considered opinion, and I find, that the capital costs of entry into the production of heavy duty wheels exist to a significant degree and are in fact substantial. [75]

2. Economies of Scale

224. The record indicates that those firms which produce a higher volume of wheels and/or wheel components have lower costs. Whether this presents an economy of scale barrier depends upon how significantly greater the cost advantages are for the high

volume producer and also what percentage share of the market a firm needs to acquire in order to operate at a minimally efficient scale. (Mann 5677.)

225. The witnesses agreed that automated equipment would lower the costs of manufacturing wheel components.

226. Witness Looney of Reyco, a drum producer, would not describe his foundry as automated and when asked whether Reyco could obtain lower overall manufacturing costs by automating, stated "on the high volume type trailer drum, I think we could, yes." (Looney 1801.) He also said that Reyco had decided not to start producing a center portion of the heavy duty wheel because feasibility studies indicated the company could not compete with existing automated suppliers costwise. "To substantiate that investment you would have to have a very high volume and a very automated type production equipment." (Looney 1802.) Witness Looney believed that DW had the lowest prices in the industry.

227. Mr. Mitchell of DW testified that "The production of high production automative-type castings that I am familiar with require automated equipment to be competitive." "It is the most economical way to go." (Looney 1824; Mitchell 2534-35.) [76]

228. Witness Rupert of Erie did not believe that most steel foundries would have the necessary automated molding equipment required to produce heavy duty wheel castings. (Rupert 788-89.)

229. Mr. Smith, formerly of Webb, doubted that many gray iron foundries could produce competitive drum castings in the volume necessary for the heavy duty truck industry because of a lack of mechanization. (Smith 937.) Mr. Smith felt that Webb's wheels had been priced too high for the high volume purchasers such as Fruehauf because the company did not have its own source for brake drum iron castings and because it had a low production steel foundry. When he asked how his foundry compared to DW's or Gunite's, he replied, "Our foundry prior to 1969 would run roughly 50 man hours per ton of wheel castings against DW or Gunite 11-12 man hours per ton." After Webb automated a jobbing foundry in 1972, its costs dropped to a range of 18-20 man hours per ton. This was still noncompetitive, according to Mr. Smith. (Smith 943-45.)

230. The record indicates that for wheels and/or drums, the minimum efficient scale is production of between 200,000 and 300,000 units per year. Mr. Greenberg, the foundry expert, estimated that the minimum efficient scale plant should produce 300,000 heavy duty wheels a year, which would be at slightly lower unit costs than the production of 200,000 units per year. (RX 280B.)

231. Mr. Rupert of Erie testified that 10,000 wheels per month is

the minimum number required to warrant automated equipment. Apparently Erie is not operating at a minimum efficient scale, since Gunite, which has more automatic molding and machining equipment than Erie, has slightly lower costs. (Rupert 779, 790.) [77]

232. Webb had considered building a foundry in 1965 which would have had a capacity of 20,000 wheels per month and matching brake drums to support that wheel production.

233. The witness from Reyco estimated that in 1972 the Reyco plant, "all out on a 2 1/2 shift basis," could produce 30,000 drum castings a month. (Looney 1821-23.)

234. On the basis of average heavy duty wheel production for the years 1972-1974 of 3.38 million (CX 717A), the smallest estimate (Rupert's) represents approximately 3.6 percent of the heavy duty wheel market and the Greenberg estimate of 300,000 approximately 8.9 percent. If a firm must have between 5 percent and 10 percent of the market to produce efficiently, a moderate to significant economy of scale barrier exists. (Mann 5677.)

235. There is little evidence in the record in regard to unit costs for disc wheel producers. Although not conclusive, one could infer that because there are only three main producers of the heavy duty disc wheel and because each produces out of only one plant, that a high volume plant is an efficient scale plant. (Zart 1187; Krauss 2358; Nelson 6418.)

3. Absolute Costs

236. Aside from foundry know-how, entry into heavy duty wheel production presents no absolute cost problem. There are no patent impediments (Mann 5715) and there is no indication in the record that any heavy duty wheel producers control any essential raw materials. Heavy duty wheel designs either can be copied from wheels on the market or can be obtained from an OEM. (Clem 2730-31; Chieger 2274.) Product liability can be adequately handled by insurance. (Rupert 793; Mitchell 2540.) [78] Most truck tractor OEMs have their own line of wheels and wheel designs. (Mitchell 2520.) The actual testing of the wheels is usually done by the user (Rupert 791-92), although wheel testing facilities, such as those of Budd, are also available on a contract basis. (Krauss 2418-19.)

237. As to technology, a wheel spider is a very difficult casting to make. It has a core, a thin wall and a complex shape and it is difficult to feed. It is difficult "to provide a good pouring and gating practice that will give you a good casting, and people that have tried to make wheels have found this out to their sorrow. So this kind of a

casting requires a foundry of good technical capability." (Rupert 785; Greenberg 4705.)

238. In the opinion of Erie's President, "your best teacher [for new wheels] is past experience." (Rupert 792.) He believed it would take foundries going into heavy duty cast spoke wheels "a long time to perfect the system to where they would perform adequately." (Rupert 786.) Webb's former official, Mr. Smith, stated that a firm entering the market could acquire the necessary technology either through "long, hard experience" or by hiring away one of but a few experts from a competitor. (Smith 950-51.)

239. To operate a drum foundry also requires persons with considerable skill. (McCorry 1858.) Specifically, managing a heavy duty drum foundry requires supervisory personnel with experience and a knowledge of the metallurgy of these items. (Fairchild 1640-41; McCorry 1861.) Such skilled persons are difficult to find. (McCorry 1858.)

240. The record reveals instances where attempted entrance into the heavy duty wheel market has resulted in failure. Nabors Trailer Co. and Roger Brothers Corporation tried to produce cast [79] spoke wheel spiders but abandoned their attempt after experiencing problems. (Rupert 796-97; Davis 1418.) And years ago, Sterling Foundry in St. Louis, a general steel foundry, tried to produce heavy duty cast spoke wheels but made no significant penetration of the market. (Mitchell 2535.)

241. McConway and Torley, a producer of castings for the railroad industry attempted to enter the heavy duty wheel market. (Smith 932-34; Mitchell 2535; Clem 2722-35.) Before its attempt to produce heavy duty wheel castings, McConway and Torley anticipated no problems in making the wheel casting (spider). (Clem 2733.) However, despite McConway and Torley's experience with very large castings, it had severe problems in making the spider casting. (Clem 2733.) Mr. Clem of McConway and Torley testified there are "literally thousands of variables" and that "the ability to feed a wheel is unique." (Clem 2733.) McConway and Torley eventually became marginally profitable in the manufacture of cast spoke wheel castings but only after contracting to supply Webb, a firm already in the industry, with rough castings and receiving reciprocal assistance in design and production from Webb's technicians. (Clem 2734, 2736-37.) With Webb's assistance, McConway and Torley's scrap rate was cut dramatically. (Smith 933-34; Clem 2734, 2753-54.) McConway and Torley sold their heavy duty wheel equipment to Webb, who moved it, retooled it and thereafter very successfully used it to produce heavy duty wheel spider castings. (Smith 934.)

242. Neither McConway and Torley, nor Reyco and Durametal, heavy duty drum producers, believe that firms such as theirs have sufficient abilities to be able to make money in the manufacture of cast spoke wheel spiders. (Fairchild 1640; Looney 1802; see Mitchell 2535; Clem 2740.) However, both [80] Mr. Looney of Reyco and Mr. Brosnahan of Ford indicated their belief that their companies presently possess the technical know-how to make heavy duty wheels. (Looney 1802; Brosnahan 4547-48.)

. 243. While the supply of technical experience is limited (Smith 950-51), such assistance is available (Smith 950; Jones 1286; Clem 2734), either from people already in the industry or from a foundry consultant. And while compensation contests could arise, there is no evidence that such costs would be unequal or discriminatory for both the firms in the market or new entrants.

4. Product Differentiation

244. Product differentiation appears to be of relatively small importance as regards heavy duty wheels. Respondent claims that this factor is nonexistent, while even complaint counsel view it as low to moderate.

245. Brand loyalty plays no significant role in this producers' goods market. (Mann 5716-17.) However, despite the existence of independent distributors, it is important to a manufacturer and seller of heavy duty wheels to have a distribution and sales network that provides contacts at the original equipment and fleet levels. (Rupert 797; Smith 954; Fisher 1387; Kenney 2099-2100.) This permits the manufacturer to provide nationwide service in case of an accident or failure. (Rupert 797.)[31] [81]

246. It is also important to be perceived as a reliable source of supply. (Kenney 2100.) It takes a significant period of time before a new manufacturer is accepted in the marketplace. The production of heavy duty wheels requires some testing facilities to assure product quality and performance. (Rupert 791-92; Smith 954; Fisher 1321, 1362; Krauss 2369-71.) Such tests are necessary as wheel failure is a cause of concern to vehicle producers since it exposes them to liability in case of loss of cargo or life due to wheel failure. (Rupert 792-93; Kenney 2099.)

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[31] Rockwell has a sales force that calls on fleets and also about 100 distributors. (Fisher 1385, 1387.) Rockwell started an aftermarket distribution system because "the vast majority of trailer manufacturers did not have a service sales outlet and Rockwell was just not getting its service parts to the end operator" and this situation still exists to some extent. (Fisher 1343-44.) DW has about 50 distributors, some with multiple branches. (Mitchell 2588.) Erie has 84-90 distributors, some with multiple branches. (Rupert 838.) Kelsey-Hayes had 208 distributors around the country in 1972. A few of these distributors were able to service both trucks and trailers. (Rowan 2059.)

5. Profitability

247. Both the respondent and Commission counsel adduced evidence concerning profitability in the heavy duty wheel market. I have studied this evidence, and the proposed findings of the parties, and have been unable to arrive at any definitive conclusions on this point. My best judgment is that the return on investment in heavy duty wheels is roughly equal to that for manufacturing in general, approximately 10 percent. (Mann 5738, 7486–7515 *in camera;* Nelson 6437–38, 6452–76 *in camera,* 6491–96 *in camera;* Smith 948–49; tr. 1874–75 *in camera;* Rowan 1954; MacDonnell 2034–35; CX 579 D, E, L, M.) [82]

C. *Potential Entry*

1. Market Environment

248. As spider manufacturers, DW has been in the heavy duty wheel market since World War I, Webb since 1946, and Erie since 1925. (Rupert 768; Smith 913; Mitchell 2507; see Vause 2189.) Gunite began making wood spoke wheels in 1909 for the infant automotive industry and progressed with the industry into the manufacture of cast spoke wheels. (CX 65F.)

249. No witness knew of any significant entry into the production of discs for heavy duty disc wheels or heavy duty rims within the last ten years. (Zart 1235, 1242; Krauss 2377.) Motor Wheel has been engaged in the production of discs for heavy duty disc wheels since the early 1930's. (Kenney 2081.) Budd has produced discs for heavy duty disc wheels since prior to World War II. (Krauss 2358.)

250. Firestone has made rims for cast spoke wheels since 1906, Goodyear since the 1930's, Redco since 1961. (Zart 1186; Sechrist 1870; Kenney 2081.)

251. Most of the producers of heavy duty drums have long been in the market. (Phillips 1569; Fairchild 1629; Looney 1793, 1799; McCorry 1836, 1840; Krauss 2358.) There has been some entry into heavy duty brake drums and hubs in the last ten years but such entry has been confined to entry by producers of other finished heavy duty wheel components with one exception. (Fisher 1315; Looney 1824; McCorry 1847–48; Kenney 2149.) Kershaw entered the production of finished hubs and drums in 1969; such components are produced for sale as part of its axles. (Davis 1408–09, 1429.) [83]

252. One firm has exited from the heavy duty wheel market in the last ten years, namely J&J Castings. J&J started making heavy duty brake drums in 1970 and stopped in June of 1973. (Jones 1267.)

253. There have been periodic shortages of heavy duty wheels since World War II. These occurred in 1946, 1966, 1968-69 and 1973-74. (CC's 1st RACF - #116; Allen 184; Rupert 798; Smith 931; Zart 1233; Rowan 1926-28; MacDonnell 2032-33; Kenney 2093; Mitchell 2541; Clem 2724; Fontaine 3580; Dahl 4136; Flagan 5153-54.) The shortage in 1973-74 considerably disrupted trailer production and may have been the most severe. (Bachman 52; Allen 184; Stein 341; Rupert 798; Smith 931-32; Fisher 1337-38; Davis 1411, 1414-15; Phillips 1567; McCorry 1843; Rowan 1926-28; MacDonnell 2032; Kenney 2086; Krauss 2372-73; Fontaine 3578-81; Dahl 4078; Flagan 5160-61; Zarella 5964-65.)

254. Fruehauf, Strick, Heil, Mack Truck and others encountered shortages of wheels in 1973-74. (Bachman 52; Allen 184; Flagan 5161; Zarella 5965.) At that time, vehicle production was curtailed and even temporarily halted due to lack of heavy duty wheels. (Tr. 1226-28 *in camera;* Rowan 1928-29; Krauss 2373; Flagan 5161; Zarella 5965; see Mitchell 2544-45.)

255. During the 1973-74 shortage of heavy duty wheels, Fruehauf, Strick, Ohio Body, Great Dane, Mack Truck and others sought alternative sources of heavy duty wheels and found them difficult to locate even though they were willing to pay a premium for wheels. (Bachman 52-53; Stein 341-42; Reeve 870-71; Zart 1257; Zarella 5965; see Mitchell 2542.)

256. Foreign sources for finished heavy duty wheel components and for castings were either unavailable or were unsatisfactory due to long lead times required; communication difficulties; shipping delays due to the distance involved; quality problems; [84] premium prices; or problems in adapting the foreign wheel for U.S. use. (Zart 1233-34; Fisher 1337-39; Davis 1422; Krauss 2374; Zarella 5964-65.)

257. The record discloses the existence of firms that have attempted to enter the heavy duty wheel market in the past fifteen years and have failed. Such failures include Hutchens, McConway and Torley, U.S. Steel and A.O. Smith. (Rupert 794; Smith 955; Fisher 1391; Looney 1803; Kenney 2107-09; Vause 2190; Chieger 2313; Mitchell 2535, 2594; Fontaine 3576-78; Flagan 5151-52.)

258. Hutchens, which is one of the nation's most sophisticated welding operations, attempted but failed to successfully enter three times, once with a cast spoke wheel and twice with a fabricated wheel in the configuration of a cast spoke wheel. (Rupert 794-96, 821; Smith 955-57; Kenney 2107-08; Vause 2191; Mitchell 2535, 2594; Flagan 5151-52.) Fontaine Trailer purchased 1200 fabricated wheels from Hutchens in 1971-72 but ceased purchasing them because the price of the cast spoke wheel again became competitive. (Fontaine

3576-78; see Smith 956.) Hutchens' fabricated heavy duty wheels experienced fatigue failures which made them unsuitable for use. (Rupert 795, 821; Smith 956-57.) Hutchens does not now make heavy duty wheels. (Looney 1805; Vause 2190-91.)

259. McConway and Torley, a supplier of large castings to the railroad industry, attempted to enter with a cast spoke wheel in cooperation with Fruehauf but was unable to produce a high quality wheel at a competitive price. (Rupert 794; Smith 932-33; Kenney 2109; Vause 2191; Mitchell 2535; Clem 2722; Flagan 5152.) A.O. Smith attempted to develop a fabricated steel wheel within the past ten years but may have never sold any wheels. (Kenney 2109.) U.S. Steel attempted unsuccessfully to produce a fabricated steel design heavy duty wheel in the mid to late 1960's. (Vause 2191-92.) [85]

260. Several producers of other heavy duty wheel components have considered production of cast spoke wheel spiders.

261. Reyco considered making cast spoke wheel spiders but decided against it because Reyco could not compete cost-wise. (Looney 1801-02, 1816, 1819.)

262. Kershaw considered acquiring the cast spoke wheel spider patterns placed at Texas Foundry by Nabors Trailer. (Davis 1417-18, 1456.) Since the patterns were obsolete and production required a long lead time, Kershaw decided not to pursue it. (Davis 1417-18, 1456-57.)

263. Alcoa made cast aluminum spoke wheels at one time but ceased. (Rupert 831.)

264. To enter into cast spoke spider casting would require a steel, malleable or ductile iron foundry rather than a gray iron foundry. (Rupert 782-83, 804, 844; Smith 967.) Each of the cast wheel spider producers, save one, uses steel castings. (Rupert 781; MacDonnell 2014; Mitchell 2507; Greenberg 4657.) Erie, the only producer of nonsteel spiders, has made both malleable and ductile iron wheels but is phasing out of malleable. (Rupert 781.) Erie switched to ductile because of its superior metallurgical properties and its lower propensity to have foundry defects. (Rupert 781-82.)

265. Currently, cast spoke spider castings are produced by the finished wheel producers for their own use. (Mitchell 2516-17.) These producers generally do no casting other than for wheel spiders. (Smith 981; Mitchell 2527, 2534.) Webb purchased spider castings from 1968 to 1973 but these were purchased from DW or Gunite. (Smith 934-35; Vause 2203.) Webb also purchased spider castings from Japan in 1973-74. (Smith 969.) Such purchases from Japan have ceased as it became uneconomical to continue them. (Smith 994.) [86]

266. Only a few steel or ductile iron foundries have the capability by virtue of their equipment and quality control and the required size of molding equipment to make a cast spoke wheel of malleable or ductile iron or of steel. (Rupert 784-87, 789; Mitchell 2533.) Steel jobbing foundries generally do not have automated equipment of a capacity to handle wheel castings economically and are unlikely candidates for entry. (Smith 937, 960-61, 988; Greenberg 4684.)

267. Very few steel foundries can economically produce a wheel due to the difficulty of the casting. (Rupert 785-86; Smith 933, 937; Mitchell 2533.) Most steel foundries produce products which do not require automated equipment. (Rupert 788-89; Smith 937; Mitchell 2534-35.) For example, Howmet Division of Crucible Steel, a large steel foundry, has produced wheel castings for Mack Truck as an accommodation for a large customer. (Greenberg 5036-37.) These castings are for off-highway use only, produced in very limited volume on a nonmechanized line and it is questionable whether Howmet considered it a profitable venture. (Greenberg 4687; Zarella 5966-68.)

268. Jobbing foundries that produce special alloys are not suitable sources of heavy duty spider castings due to contamination problems which makes machining very costly. (Smith 991-92.)

269. Prior to the expansion of the Gunite plant, Mr. Greenberg examined existing foundries on behalf of Gunite, such as Crane Chattanooga Foundry, White Farm Equipment in Charles City, Iowa and Waupaka Foundry, and considered acquiring one of the plants or some of the equipment but found each unsuitable. (Greenberg 4599A, *et seq.*) Therefore, Kelsey-Hayes internally expanded its Gunite wheel manufacturing facilities at a cost of $25 million. (CX 660Q.) [87]

270. Mr. Smith of Webb testified that, during the shortage of heavy duty wheels in 1973-74, Webb searched for an alternative supply of steel castings and found only McConway and Torley. (Smith 932.) Mr. Clem testified that to his knowledge no steel foundry has evidenced any interest in entering heavy duty cast spoke wheels since 1968. (Clem 2764.)

271. Ford, GM, Chrysler, Deere & Company, IHC, J.I. Case, White, Caterpillar, Lynchburg Foundry, Neenah Foundry, Rockwell and Waupaka do not possess the equipment to cast steel wheel spiders. (Brosnahan 4554; Greenberg 4684-4685, 4690-91.)

272. To enter production of drum castings requires a gray iron foundry, except for the production of centrifuge type drums. (Rupert 810; Looney 1798, 1800; McCorry 1835; Kenney 2084-85; Krauss 2356; Mitchell 2500, 2526; Clem 2728.) The manufacture of centrifuge

brake drums is peculiar and requires a particular type of foundry. (CX 40P; Kenney 2085, 2093.) Centrifuge type drums represent less than 10 percent of the market and have been declining in popularity, face an uncertain future and are more expensive. (Smith 914-15; tr. 2086-87; 2171, 2173 *in camera*.) Only Motor Wheel and DW make centrifuge type heavy duty drums. (CX 40P; Smith 914; Kenney 2085.)

273. Not every gray iron foundry can economically manufacture a brake drum because of required tooling, training and the necessary degree of automation. (Smith 937; McCorry 1860-61.) The manufacture of heavy duty drum castings requires proper size equipment, without which there are serious quality problems. (Fisher 1340.) Currently, almost all heavy duty drum castings are produced in foundries dedicated extensively or almost entirely to the production of such castings or hub castings. (Phillips 1563-64; Fairchild 1625-1626; Looney 1820; McCorry 1835-36, 1855.) [88]

274. Gray iron jobbing foundries are unlikely candidates for entry into heavy duty drum castings due to their lack of automated facilities and, frequently, their limited size capacities. (Smith 937; Greenberg 4686; see Fisher 1330.) Gray iron jobbing foundries also require core-making equipment and cleaning equipment not needed for heavy duty drum production. (Looney 1801.) A gray iron jobbing foundry would have higher costs in producing heavy duty drums than would a specialized drum casting foundry. (Fairchild 1625-26.) When J&J Castings sought a foundry to make its heavy duty drum castings, it was turned down by U.S. foundries because they could make more money by producing other simpler castings. (Jones 1270.)

275. J&J Castings in 1970 and 1973 and Rockwell, Motor Wheel and Webb in 1973-74 experienced difficulty in obtaining heavy duty hub and drum castings. They found that domestic producers were at full capacity and foreign producers in Japan and Europe had quality, delivery and cost problems. (Smith 931-32, 959; Jones 1269-70; Fisher 1337-39; Kenney 2094.) Webb, Reyco, Standard Forge and Budd also turned to a foreign drum casting supplier only in times of intense shortage when they could not find a sufficient supply in the U.S. (Smith 930; Phillips 1567-68; Looney 1822, 1830-31; Krauss 2374.) Foreign made hub and drum castings today are more expensive than domestic made castings.[32] (Smith 930; Fisher 1341; Krauss 2374). Kershaw found that, after Gunite returned Kershaw's heavy duty drum patterns, it had little success finding another foundry to replace Gunite as a source of these castings including the

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[32] Motor Wheel formerly purchased hub forgings abroad but no longer finds it economical. (Kenney 2109-10.)

foundries of its parent, Dana. (CX 231; Davis 1410-11, 1415-16, 1444-46, 1461.) [89]

276. Heavy duty brake drum and hub castings are both made and purchased by the producers of finished drums. (R's 2nd RAF - #145; Rupert 839; Fisher 1324, 1335-36, 1340-42; see Davis 1409-11; Phillips 1566-67, 1575-76; Fairchild 1625, 1641; Looney 1831; tr. 2090-91 *in camera,* 2093; tr. 2153 *in camera;* Vause 2203, 2231-33; Krauss 2356; Mitchell 2517.) There are a number of gray iron foundries which supply only castings to various drum producers. (Bennett 289-90; Smith 936, 967; Looney 1822; Kenney 2094; tr. 2411-12 *in camera;* Mitchell 2517-18.) Other than General Foundry, these firms generally make only a few of the required castings, namely, the odd sizes and slow movers. (R's 2nd RAF - #44, 45, 47; Fisher 1337, 1339; Looney 1831; McCorry 1847; tr. 2091 *in camera;* Krauss 2363.) Several of the suppliers of heavy duty drum castings have exited from this product market. (Phillips 1566; Fairchild 1626-27.) Thus, there are but a limited number of drum casting suppliers who would be possible entrants into the area of finished heavy duty drums.

277. So far as significant entry into the production of heavy duty wheels, Mr. Kenney of Motor Wheel testified that he does not foresee any new entry in either cast spoke wheels, disc wheels or components thereof. (Kenney 2094, 2107.) Ford Motor Company has no plans to enter the heavy duty wheel market. (Brosnahan 4554.) None of the vehicle producers including GM, Ford, IHC, Mack Truck and White Motor Company have made cast spoke wheels or discs. (MacDonnell 2017-18; Krauss 2375; Mitchell 2516; Brosnahan 4554.) Mack Truck has never considered going into the production of heavy duty wheel discs or spiders. (Zarella 5968, 5973.) These vehicle producers lack the ability to produce heavy duty cast spoke wheels as they are not equipped and designed to produce heavy duty spoke wheels. (Mitchell 2536.) [90]

2. Fruehauf as a Potential Entrant

278. Prior to the acquisition of Kelsey-Hayes, Fruehauf was dependent on outside sources for the heavy duty wheels it used on all of the trailers it built. (CX 139A.) The company was motivated to integrate into heavy duty wheels so as to ensure a source of supply of a vital commodity in times of shortage. (CC's 1st RACF - #60; Flagan 5153-54.)

279. In addition to cost savings, it would also be to Fruehauf's advantage to manufacture its own wheels because scheduling,

manufacturing and shipping would then be under its control, not subject to supplier, labor, or other problems. (CX 139B; Rowan 1904.)

280. Fruehauf has made it a practice to encourage new sources for wheels. (Flagan 5153-54). Its interest in the heavy duty wheel market has been continuous since the late 1960's. At that time, Webb proposed supply arrangements, including a joint venture, in which Webb would guarantee Fruehauf a supply of wheels. Fruehauf responded with interest but these talks were terminated due to a lack of interest at the corporate level of Webb. (Smith 941-42; 979-80.)

281. Fruehauf had sufficient research and development capability and test facilities to develop a new heavy duty wheel and it wanted to develop such a wheel for weight and cost reasons as well as to enhance the availability of wheels. (Rowan 1924, 1930; Chieger 2274; Flagan 5088.) As stated by Mr. Chieger, Fruehauf sought to develop a wheel "that would be competitive with a cast wheel with the same performance level as the cast wheel." (Chieger 2277.) [91]

(a). *Fruehauf's Fabricated Aluminum Wheel*

282. Fruehauf initiated development of an extruded aluminum wheel prior to March of 1967. The company sought to develop an aluminum spider and hub assembly as well as a compatible drum assembly. This project did not seek the development of the rim necessary to complete a heavy duty wheel. (CX 168, CX 176, CX 183B.)

283. The purpose of the aluminum wheel project was "to provide a trailer wheel of our design, made from Decatur [Fruehauf] extrusions and allowing fabrication in our manufacturing plant. Wheel assembly to be lower in cost and lighter in weight than existing product." (CX 161A; see CX 104B; CX 163A.) This project also was to produce a heavy duty wheel that was true running, had a minimum tooling cost, had improved method of brake drum or disc attachment and provided an additional source of supply. (CX 135C). Fruehauf envisioned that the program would provide an 80 pound per axle weight saving and a $12.00 per axle cost saving. (CX 166; Flagan 5115.)

284. In May of 1970, Fruehauf prepared analyses of the cost of production of 100,000 wheels per year on a two shift basis for equipment and tooling, overhead, manpower, depreciation and facilities requirements, with the resultant cost per wheel estimated at $19.71 for an investment of $778,000. (CX 145; CX 148A-C; CX 149A-B; CX 150; CX 151; CX 153A-B; CX 154; CX 155; CX 156; CX 157A-B; CX 158A-B; Flagan 5116-17.) To produce 200,000 wheels per

year was estimated to require about $1,500,000 of investment for facilities and equipment. (CX 154.) [92]

285. Testing on the aluminum wheel was performed during 1970-71 by Fruehauf in order to assure that the wheel would perform satisfactorily. (CX 124A-B; CX 125; CX 126; CX 127; CX 128; CX 129; CX 130; CX 131.) The testing included running the wheel through 2 million cycles at 22,270 foot pounds of side pressure without cracks, executing brake stops on the extruded aluminum wheel and brake drum assembly, assessing the effect of stress risers, assessing whether there was heat checking and determining fatigue strength. (CX 125, CX 126, CX 127, CX 128, CX 130, CX 131.) The testing also included a cornering fatigue test and abuse with hand tools. (CX 177; CX 178.) Fruehauf's extruded aluminum wheel satisfactorily passed the testing program to which it was subjected, including the cornering fatigue test. All technical aspects of the system design indicated that it could service the trailer industry but it was felt the manufacturing costs would exceed costs of purchased cast wheels. (CX 160D-F; CX 179.)

286. Fruehauf's plans called for it to produce the wheel either with a large extrusion press purchased from Dow Chemical or by running the wheel at the Fruehauf Decatur plant as a series of extrusions later to be welded together. (Flagan 5141.)

287. The program included development of a drum as well as an extruded aluminum spider. (CX 146A-C; CX 168; Flagan 5118, 5167.)

288. Fruehauf's aluminum wheel project succeeded in reducing weight by about 80 pounds per axle, (CX 160B) which was a weight advantage over the cast spoke wheel Fruehauf was then using. (Flagan 5174.)

289. In early 1971, Fruehauf concluded that the aluminum wheel would cost $3.68 more than the cast steel wheel then being purchased. (CX 147A-B; CX 152; CX 188A; Flagan 5121-22.) [93]

290. Even at this price, the projected cost of Fruehauf's extruded aluminum wheel was substantially lower than that of Alcoa's aluminum disc wheel. (Flagan 5174.) The weight savings may make an aluminum wheel desirable to the user even at a premium price as users desire weight savings which enable them to carry greater payloads and reduce their fuel costs. (Kenney 2176.)

291. Fruehauf admittedly would consider making a higher cost item with a superior feature if that feature were worth it to the customers. (Flagan 5175.)

292. In 1971, Fruehauf decided to close out the aluminum wheel project due to its higher cost, but to maintain the project's files to permit introduction of the wheel into the market if market

conditions should change. (CX 160E-J; CX 162; CX 180; CX 181; Flagan 5123.)

293. Fruehauf's Mr. Flagan testified that if the price of wheels to Fruehauf were to rise (50 percent), "it would change the whole picture" as to its entry into heavy duty wheels. (Flagan 5159-60.) Since 1970 the prices of heavy duty wheels have risen substantially. (Rupert 793, 832; Kenney 2097-98; Mitchell 2541.) However, Mr. Krauss of Budd was of the opinion that because of the large amount of labor involved, a fabricated wheel would still be uneconomical. (Krauss 2416.)

(b). *Fruehauf's Fabricated Steel Wheel*

294. In the late 1960's, Fruehauf began a project to develop a heavy duty fabricated steel wheel similar in appearance to a disc wheel. It was composed of a hub center and rim band, two flat discs, thus differing somewhat in design from a traditional disc wheel. (Chieger 2331-32; Flagan 5102-03.) [94]

295. The purpose of developing the fabricated steel wheel was to develop a wheel that passed all physical and economic requirements for Fruehauf for possible replacement of the present cast wheel. (CX 135B.) The steel fabricated wheel was envisioned as having the characteristics of light weight; heavy duty construction; true running, demountable rims; and improved method of brake drum or disc attachment; easily automated steel design; and a savings of $4.00 per wheel. Such wheel was also envisioned as a source of supply for Fruehauf. (CX 135C.)

296. Fruehauf developed several prototype fabricated steel wheels in early 1969. (Flagan 5103-04.) Such prototypes incorporated the "tru-track principal" which was a patentable feature unique to this fabricated steel wheel. (CX 123; CX 136.)

297. The fabricated steel wheel developed by Fruehauf was given several performance tests and passed a dynamometer test. (CX 117A-B; CX 118A-B; CX 210; Flagan 5105.)

298. In May 1970, it was reported with respect to the steel fabricated wheel that the "final design achieves all goals established at outset of project. We have a fabricated steel wheel suitable for Fruehauf production that is within one pound of the cast wheel weight with a cost advantage of approximately $6.00 per wheel; that can be used with or without the tru-track principal for run out control; that has more than adequate fatigue life and looks good." (CX 132C; Flagan 5108.)

299. As part of the steel fabricated wheel project, Fruehauf developed manufacturing costs. (CX 137A; CX 211.) However, such

costing neglected to include the necessary bearing cups, and after several costing adjustments the fabricated steel wheel was estimated to cost $1.95 more than Fruehauf was paying at the time for cast spoke wheels without any allocation for profit. (CX 188A; Flagan 5109, 5122.) [95]

300. Fruehauf stopped work on the steel fabricated wheel as of March 1, 1970 in order to pursue development of the weight-saving aluminum wheel as "the most logical first Fruehauf wheel." (CX 135F.) It was believed that the aluminum wheel had better potential to achieve its goals. (Flagan 5107-08.)

301. However, Fruehauf maintained sufficient records to resurrect the fabricated steel wheel project. (CX 135F.) As Fruehauf's Mr. Flagan reported, "I want to be in a position to resurrect these programs, should the economic conditions change in the future to where the programs can be competitive. Therefore, make sure that everyone involved in the project does a thorough job of summarizing past results and present position, as well as future needs of the program, so that we do not have to try to reconstruct the program complete from bits and pieces, should we desire to resurrect it." (CX 162.)

(c). *McConway and Torley Wheel*

302. In 1967-68, on the occasion of a strike against DW's wheel operations, McConway and Torley made a market study and decided to diversify into the wheel business. (Clem 2724-25.) McConway and Torley sought out Fruehauf, a leading heavy duty wheel purchaser anxious to add an additional source of supply. (CX 597A-J; Clem 2724-26, 2748-49; Flagan 5152; see Mitchell 2542.) Fruehauf's backing was sought as it was the largest trailer manufacturer and therefore "could provide us (McConway and Torley) with the type of volume that we were seeking." (Clem 2725-26.) Fruehauf encouraged McConway and Torley in its new endeavor. (Clem 2726; Flagan 5152.) [96]

303. McConway and Torley had entered the steel foundry business in 1884 and at the time of its entry into the wheel market was involved in casting 450 pound railroad freight car couplers and coupler yokes. (Smith 933-34; Clem 2722-23.)

304. McConway and Torley began the production of cast spoke trailer wheels in 1969 and ceased production in 1974. (CX 600A-E; CX 602A-J; CX 604A-B; CX 605; CX 608; CX 609; Clem 2723-24; Flagan 5152-53.) From 1969 through late 1973 McConway and Torley produced finished spiders for Fruehauf and acquired the balance of the parts necessary to produce a complete wheel assembly first from

DW and subsequently from Webb. (CX 600A-E; CX 602A-J; CX 604A-B; Smith 932; Clem 2723-24, 2728-29, 2735, 2753.) From 1973 until McConway and Torley exited from the market in 1974, McConway and Torley's involvement in heavy duty wheels consisted solely of supplying unmachined spider castings to Webb to whom it had sold its equipment for machining wheels. (CX 605; CX 606; CX 607A-B; Smith 934, 983; Clem 2724, 2735, 2738.)

305. McConway and Torley did none of the original engineering on the cast spoke wheel including its components (Clem 2729-2731), nor did it have any engineering staff for the cast spoke wheel. (Clem 2731.) Fruehauf furnished McConway and Torley with the design and prints as well as the money to buy patterns and equipment. (Clem 2731.) McConway and Torley was restricted in its use of the Fruehauf tooling and thus could produce wheels only for Fruehauf because the tooling was designed for the unique Pro-Par axle. (Clem 2725-27.) McConway and Torley did not have any facilities to test the design of the wheel; instead, Fruehauf had the testing equipment and performed all of the tests. (CC's 1st RACF - #50, 55; Clem 2731; Flagan 5152, 5155.) [97]

306. Fruehauf provided McConway and Torley with numerous suggestions as to improvements in the design and manufacture of the wheels. (CC's 1st RACF - #50; CX 106A-B; CX 107; CX 108; CX 110A-B; CX 111A-B.)

307. McConway and Torley's wheels were tested favorably against those of Gunite and DW (CX 112Q; CX 113) but as Fruehauf's engineers noted, "the placement of chills and vent holes in the mold is another long tedious hand operation that makes one wonder if they make a wheel economically and consistently from mold to mold." (CX 105A.) Furthermore, during its association with Fruehauf, McConway and Torley was experiencing an extremely high scrap rate on its wheel castings and other productivity problems. Thus the operation was only marginally profitable at the time of the company's departure from the market. (Smith 933; Clem 2732-34, 2736-37.)

308. The project ended because the McConway and Torley wheel was no longer competitive. (Chieger 2276.) McConway and Torley could not successfully produce a good casting and do so economically. "They ran very high scrap." (Smith 933.)

(d). *U.S. Steel Wheel*

309. A few months following the termination of its internal wheel efforts, Fruehauf entered into a program with United States Steel Corporation (hereinafter "U.S. Steel") in which Fruehauf was

to test and evaluate for U.S. Steel a steel fabricated wheel designed by an outside engineering firm. (CX 219; Flagan 5157.) The project was undertaken at Fruehauf's suggestion to have an opportunity to participate in the development of a steel wheel and, if the wheel proved to be successful, to have an alternative supply source for a steel wheel. (CX 216; CX 217; CX 218; CX 219; Flagan 5157.) U.S. Steel was [98] looking for a development program to aid in marketing steel and Fruehauf encouraged U.S. Steel to look at wheels. (Flagan 5157.)

310. The U.S. Steel fabricated steel wheel project began at Fruehauf in February of 1973 and ended in September of 1973. (CX 114A-C.) U.S. Steel supplied fabricated steel wheel prototypes to Fruehauf for testing. Fruehauf tested these prototype wheels at a discount from what it would have charged others to encourage U.S. Steel to continue the program. (Flagan 5157-59.)

311. Tests conducted showed that the U.S. Steel wheel was inadequately designed and was unacceptable for commercial use. (CX 115A-E; CX 116; Flagan 5157.)

312. Based in part on its tests, Fruehauf made design recommendations to U.S. Steel. (CX 114A-C; CX 220). Subsequent to its tests of the U.S. Steel wheel, Fruehauf proposed to U.S. Steel that it may be "to our mutual advantage to get together and develop a program using as a basis their efforts to date as well as our past effort and experience on fabricated wheel design." (CX 223.)

(e). *Perception of Fruehauf as a Potential Entrant*

313. Fruehauf's interest in entering the heavy duty wheel market was known to several of the heavy duty wheel suppliers, including at least four of the leading suppliers. (Zart 1244; Looney 1831; Vause 2204; Mitchell 2592.) Firestone's rim and disc wheel plant was visited in 1971 by Fruehauf personnel "to see how we [Firestone] made rims with the possibility of their [Fruehauf] making their own rims." (Zart 1244.) DW, Fruehauf's principal wheel supplier, was aware that Fruehauf was encouraging the entry of McConway and Torley. (Mitchell 2542.) DW also has been aware [99] for over ten years that Fruehauf has been working on a fabricated heavy duty wheel design. (Mitchell 2592.) Mr. Mitchell of DW believed that such a design could be made to perform successfully. (Mitchell 2592.) Prior to its acquisition, Kelsey-Hayes was aware that Fruehauf was working with other companies to develop heavy duty wheels. (Vause 2204.) Webb felt that Fruehauf would be interested in some arrangement (possibly a joint venture) with Webb to produce heavy duty wheels. (Smith 941-42; 979-80.)

Webb viewed Fruehauf's involvement with McConway and Torley as "a venture by Fruehauf to supply wheels for Fruehauf trailers." (Smith 932.) "Fruehauf negotiated an agreement with a contract with McConway and Torley at Pittsburg to set up McConway and Torley in the wheel business to supply Fruehauf." (Smith 942.)

D. *Potential for Vertical Foreclosure*

1. Size of the Market

314. Complaint counsel and respondent disagree on the size of the heavy duty wheel market (as depicted in Table 1) in the following respects: Respondent contends that OEM producers of heavy duty wheel components who use all of their in-house output should be included in the market for the determination of market shares and percentages of potential vertical foreclosure.[33] Logically however, for purposes of **[100]** assessing the potential for vertical foreclosure, these in-house producers need not be considered since suppliers foreclosed from selling to Fruehauf cannot readily expect to sell, at regular prices, their wheels and components to purchasers who possess captive supplies.

315. Respondent also contends that imported European heavy duty wheel products, such as those of Michelin and SKF, should be included in the market. (Krauss 2408-09; 2423.) As complaint counsel point out, Michelin and SKF accounted for probably less than one percent of disc wheel sales and thus, less than .3 percent of the overall heavy duty wheel market. (Zart 1242; Krauss 2422-23.) Moreover, the small disc wheel producers were considered by the witnesses to be specialized suppliers and thus to have a *de minimis* effect in the market. Their exclusion from the market universe does not render the statistics misleading.[34] (Krauss 2421-22; Zart 1241-42.)

2. Foreclosure

316. Fruehauf's heavy duty wheel purchases amounted to $12,177,536 or 6.5 percent of the heavy duty wheel market in 1970;

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[33] IHC produces 30-50 percent of its drum requirements. (Vause 2238-39.) GM's Truck and Coach Division machines heavy duty drums. (McCorry 1849.) Freightliner, Mack Truck, PACCAR and Utility, all produce heavy duty hubs and Utility produces both hubs and drums for in-house supply. (Bennett 289-90; CX 717C *in camera.*) If all of Utility's drum use was machined in-house, its share of the heavy duty wheel market would be very slight due to Utility's small share of the trailer market. (CX 254B; CX 632X *in camera.*) IHC's share of the heavy duty wheel market would also be small as its drum production is between 7.5 percent and 12.5 percent of truck drum usage and trucks use only 67 percent of the total heavy duty wheel market. (CX 254B; CX 632X *in camera.*) Total hub production by Freightliner, Mack, PACCAR, and Utility, all for in-house use, represented only about 10 percent of all hubs produced in 1972. (CX 717C *in camera.*)

[34] Small specialty disc producers include Motor Rim and Wheel, Standard Rim and Wheel, Wisconsin Rim and Wheel, and Southwest Rim and Wheel. (Finding 172.)

$11,599,934 or 6.0 percent in 1971 and $13,262,419 or 5.5 percent in 1972. The three year average is 5.8 percent. (CX 1B, CX 1I, CX 1G; Mann 5700-01.) [101]

317. Respondent contends that because, at the time of trial, Kelsey only produced cast wheels and drums for the trailer market (Vause 2225), Fruehauf's purchases of rims and/or discs should be disregarded for purposes of computing the potential for vertical foreclosure. This would reduce Fruehauf's average purchases to 3.9 percent for 1970-72. (Zart 1187; Nelson 6962-63; Mann 7519; CX 1D & I.) This view disregards Kelsey's ability to make discs and rims for the trailer market if they were assured a sales outlet.

318. Historically Kelsey-Hayes' principal heavy duty wheel customers have been truck and truck tractor manufacturers, which in 1972-73 included such OEMs as General Motors, Ford, IHC and Mack. (R's 1st RAF - #68; CC's 1st RACF - #12.) Kelsey's sales to trailer OEM's represented only 6.6 percent of Kelsey's total heavy duty wheel sales in 1970-72. (CC's 2nd RACF - #46; CX 45B, D-F.) Nonetheless, the cross-elasticity of supply between truck tractor and trailer wheels is "virtually infinite" (Mann 5699), a fact which lessens the importance of Kelsey's past sales in determining the potential for vertical foreclosure.

319. Trailer manufacturers testified that they believe Kelsey-Hayes would favor Fruehauf at their expense, if heavy duty wheels were in tight supply. (Rupert 803; tr. 2198 *in camera;* see also Reeve 862; Mitchell 2549.)

320. Manufacturers of heavy duty wheels expressed their opinion that there could be a curtailment of outside sales of wheels to Fruehauf as a result of the acquisition of Kelsey-Hayes. (Smith 940; Looney 1809; Fisher 1351; Kenney 2112; Mitchell 2549.) [102]

321. In 1974, Reyco sold $600,000 to 700,000 worth of drums to Fruehauf. In 1975, Reyco's sales of drums to Fruehauf were less than $50,000. Reyco perceived this decline as due primarily to a slump in the trailer market but in part to the fact that Fruehauf, through Kelsey-Hayes, was capable of supplying its own needs at the low rate of truck trailer production in 1975. (Looney 1808-09.)

322. In the past Fruehauf has relied on Dayton for cast spoke wheels and drums. Gunite's sales to Fruehauf have been small and Fruehauf purchased only 7 percent of its truck trailer wheel requirements from Kelsey in 1972. (R's 1st RAF - #72; Stipulation 8/5/75; CX 1D.) Dayton, upon learning of the Kelsey acquisition, contacted Fruehauf about the possibility that Fruehauf would cease buying from Dayton the same percentage of wheel requirements as

they had in the past. Fruehauf granted Dayton a five year renewable contract for the purchase of wheels. (Rowan 1934; Mitchell 2545-47.)

323. Expansions of facilities in the industry for the production of wheel components has taken place. (Rupert 841; MacDonnell 2034, 2062; Mitchell 2571; Krauss 2420; Looney 1822.) Therefore, respondent contends that capacity in the heavy duty wheel market is sufficient to preclude shortages for the next five years, which would minimize the effects of any vertical foreclosure. In the past, shortages of heavy duty wheels have not been foreseen. (Reeve 860; Fairchild 1659; McCorry 1843; Rowan 2033; Kenney 2093-94; Krauss 2428.) There is no foolproof method for predicting shortages. (Rowan 2033; Mitchell 2590.)

324. There is no convincing evidence in the record — beyond the statements of Fruehauf's employees — that, should there be another heavy duty wheel shortage, Kelsey-Hayes will allocate its production on a pro-rata basis among its customers. (Vause 2226; MacDonnell 3189; CX 242C, *in camera*.) [103]

325. Fruehauf has demonstrated its propensity to source in-house after vertical integration, and it would be clearly advantageous for Kelsey-Hayes to be assured of volume heavy duty wheel sales to make full use of recent expansions and to thus lower unit costs. These two factors make it reasonably probable that the full potential for vertical foreclosure (around six percent) will be realized.

VIII. LEGAL DISCUSSION

A. *Market Definition*

An indispensable initial step in any Section 7 case is the determination or definition of an appropriate "line of commerce" or relevant market. In the instant case, the existence of three relevant product markets are not in dispute. These are heavy duty antiskid braking devices, truck trailers and heavy duty wheels.

Three submarkets of the heavy duty wheel market have been alleged or proposed at one time or another in the proceeding: truck trailer wheels; cast spoke truck trailer wheels (exclusive of rims); and cast spoke wheel spiders. The truck trailer wheel submarket was alleged in the complaint (Para. 12(b)), but complaint counsel elected not to present evidence concerning it (trial brief at p. 3). The cast spoke wheel spider submarket was not alleged in the complaint, and was not litigated with the express or implied consent of respondent as required by Rule 3.15(2).[35] Thus, it is not being considered in this opinion. This leaves only the cast spoke truck trailer wheel (exclusive of rims) submarket for determination. [104]

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[35] In fact, the cast spoke wheel spider submarket was not proposed in this case until the filing of complaint counsel's proposed findings.

The complaint alleges (Para. 12(c)), and complaint counsel contend, that cast spoke truck trailer wheels (exclusive of rims) constitute an appropriate submarket within which to judge the probable competitive effects of the merger. Counsel cite various *Brown Shoe* criteria, *i.e.,* (1) industry recognition that these types of wheels are generally distinct from cast spoke wheels for trucks; (2) the existence of specialized producers; and (3) distinct characteristics of the truck and truck trailer wheels. Respondent argues, *inter alia,* that such a submarket cannot be found because of the high degree of cross-elasticity of supply between cast wheels for trucks and cast wheels for trailers.

In fact, the equipment used to manufacture cast truck wheels is the same as that used to make cast trailer wheels. (Mitchell 2521.) Both truck and trailer wheels can be and are run in the same foundry (Vause 2184), with only 20 minutes to an hour needed to convert from producing truck wheel castings to castings for trailer wheels. (Rupert 809-10; Smith 965-66.) Moreover, the machining of truck drive wheels and trailer wheels is interchangeable on the same machine line. (Vause 2225.) And three of the four leading cast wheel producers make both truck and trailer wheels. (Smith 965; Mitchell 2521; Vause 2184.)

In its decision in the *Budd* case, the Commission was similarly faced with the question of delineating submarkets in the presence of high supply cross-elasticity. There it held (86 F.T.C. 518 (1975) at 571-72):

> The ALJ, in accepting complaint counsel's argument that "closed-top" and "open-top" van trailers each constitute a relevant submarket, mechanically relied on the fact that several of the submarket criteria referred to in *Brown Shoe Co.* v. *United States,* 370 U.S. 294, 325 (1962) [105] were applicable, such as peculiar characteristics and uses, distinct prices, and industry recognition of open-top van trailers as a category of truck trailers. But as the Court observed in a later case, "[T]hese [Brown Shoe] guidelines offer no precise formula for judgment and they necessitate, rather than avoid, careful consideration based upon the entire record" *United States* v. *Continental Can Co.,* 378 U.S. 411, 449 (1964). Cross-elasticity of supply can also be an important consideration in defining markets. See *Brown Shoe, supra* at 325 n. 42. The interchangeability of production and distribution facilities between two products is a strong indication that in measuring the relevant market and the degree of market power held by firms, the output of both products should be included since the manufacturer of one can shift readily to the production and sale of the other in response to profit opportunities. *Cf. Sterling Drug, Inc.,* 80 F.T.C. 477 (1972). See also *United States* v. *Columbia Steel Co.,* 334 U.S. 495, 510-11 (1948). Because the record establishes such a high degree of cross-elasticity of production, and identical marketing ease, among van trailers, we conclude that "open-top" and "closed-top" van trailers do not constitute separate submarkets.

[106] See also *Twin City Sportservice, Inc.* v. *Charles O. Finley & Co.*, 512 F.2d 1264, 1271 (9th Cir. 1975) and *Calnetics Corp.* v. *Volkswagen of America, Inc.*, 532 F.2d 674, 691 (9th Cir. 1976).

The rationale of the Commission in *Budd* is applicable to the instant case and dispositive of the proposition that cast spoke truck trailer wheels constitute a valid submarket, in view of such a high degree of cross-elasticity of production, which was described by respondent's economist as "virtually infinite." (Mann 5699.)

B. *Anticompetitive Probabilities*

The acquisition of Kelsey-Hayes by respondent Fruehauf can be termed a "backward vertical" merger, *viz.*, the acquisition by a customer of a supplier. In analyzing the probable competitive effects of this merger, we must be mindful of settled legal precedent. In *Ford Motor Co.* v. *United States*, 405 U.S. 562, 570-71 (1972), the Supreme Court reaffirmed its holding in *Brown Shoe*, 370 U.S. 294, 323-24 (1962) that:

> The primary vice of a vertical merger or other arrangement tying a customer to a supplier is that, by foreclosing the competitors of either party from a segment of the market otherwise open to them, the arrangement may act as a "clog on competition," *Standard Oil Company of California* v. *United States*, 337 U.S. 293, 314, which "deprive[s]. . . rivals of a fair opportunity to compete." H.R. Rep. No. 1191, 81st Cong., 1st Sess. 8. Every extended vertical arrangement by its very nature, for at least a time, denies to competitors of the supplier the opportunity to compete for part or all of the trade of the customer-party to the vertical arrangement.

[107] The Supreme Court further stated in *Brown Shoe* that (370 U.S. at 328):

> * * *the diminution of the vigor of competition which may stem from a vertical arrangement results primarily from a foreclosure of a share of the market otherwise open to competitors* * *.

It is thus necessary to consider the extent of vertical foreclosure in this case, noting (1) that in *Brown Shoe* the Supreme Court invalidated a vertical merger which foreclosed only 1.7 percent to 2.1 percent of the relevant market, and (2) that in *Ash Grove* the Commission did not consider as *de minimis* a foreclosure of only 3.1 percent.[36] Both cases, of course, recognize that while the degree of foreclosure is an important consideration, it is necessary to further consider the market setting in which the merger occurred. As detailed *infra*, the evidence in this case leads me to conclude that, with respect to antiskid devices and heavy duty wheels, the foreclosure percentages involved are not *de minimis*, and that the merger occurred in a setting where concentration was high and where barriers to entry or effective competition were generally significant.

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[36] *F.T.C. v. Ash Grove Cement Co.*, 85 F.T.C. 1123 (1975).

1. Antiskid

In 1975 Fruehauf's purchases of antiskid braking devices totalled 4.7 percent of the dollar universe and 5.4 percent of the unit universe. In that year Kelsey-Hayes ranked number one in the industry and its sales of the device totalled 28.6 percent of the dollar universe and 32.5 percent of the unit universe. In 1975, Fruehauf purchased 42 percent of their antiskid requirements from Kelsey-Hayes. But in assessing the full potential [108] for vertical foreclosure in the antiskid market it must be kept in mind that Fruehauf is the most vertically integrated of all trailer manufacturers, and has a corporate policy in favor of "in-house" buying and utilization of its internally generated products. Thus, the degree of foreclosure or potential foreclosure cannot be considered *de minimis* under the ruling case law.[37]

There is a high degree of concentration in the heavy duty antiskid device market. At the time of the hearings, there were only seven active suppliers of antiskid systems. The top two firms accounted for over 50 percent of dollar and unit sales in 1975, and the top four firms for nearly 75 percent.

The barriers to entry or effective competition are significant. Economies of scale are high in this market. Capital costs estimates ranged from high to moderate, *i.e.*, from several million dollars to $14.6 million.[38] While the absolute cost [109] barrier does not appear to present much problem, elements of product differentiation are present, although this barrier is not insurmountable.

Respondent argues that the antiskid market is in its infancy, and that the data concerning it is simply too unreliable upon which to make a judgment as to probable competitive effects of the acquisition. However, there is no exemption in Section 7 based upon the newness of a market. In fact the statute is designed to curb anticompetitive behavior in its incipiency. Accordingly, we must make the best judgment we can based upon the material at hand.

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[37] It would not be reasonable, in my opinion, to use Fruehauf's 1975 purchases from Kelsey-Hayes, made during the pendency of this litigation, as the appropriate measure of foreclosure.

Additional foreclosure exists in the industry by virtue of General Motors ownership interest in AC, one of the seven suppliers. In 1975, AC provided approximately 90 percent of GM's requirements for its truck and truck tractor production. (Finding 55.)

[38] In *British Oxygen Co.*, 86 F.T.C. 1241, 1350 (1975), it was found that an initial capital investment of $7 to $8 million for a small plant and up to $16 million for a larger plant constituted a substantial entry barrier. *Rev'd on other grounds and remanded sub nom. BOC International Ltd.* v. *F.T.C.*, 2d Cir., No. 76-4044, slip. op., May 19, 1977.

Under the authorities there is no alternative to holding that a sufficient degree of foreclosure or threatened foreclosure exists in a sufficiently unhealthy market climate.

2. Wheels

Fruehauf purchased 6.5 percent of all heavy duty wheels sold in 1970, 6 percent in 1971 and 5.5 percent in 1972. On the supply side, Kelsey-Hayes was the fourth largest supplier of wheels in 1971 and 1972 with 15 percent of the market in each year. Heavy duty wheels are an essential product for the manufacture of trailers and shortages of wheels periodically curtail trailer production. There is substantial probability that Fruehauf in the future will be supplied with all or virtually all of its heavy duty wheel requirements by Kelsey-Hayes because of Fruehauf's well-established policy of buying in-house to the fullest possible extent. Thus, under ruling case law, the degree of foreclosure or reasonably likely foreclosure cannot be considered *de minimis.*

There is likewise a high degree of concentration in the heavy duty wheel market. The top four firms accounted for between 65 percent and 71 percent of the market in the years 1970 through 1972. The top eight firms accounted for between 93 percent and 95 percent of the market during that period. **[110]**

Barriers to entry or effective competition in the heavy duty wheel market are on the whole substantial. Entry at meaningful volume levels of production requires a capital outlay of some millions of dollars, with $10 million or more not unreasonable amounts. Economies of scale are significant; to be minimally efficient a plant should manufacture between 200,000 or 300,000 units per year. A salient feature of the absolute cost barrier is the fact that the manufacture of wheels requires a high degree of technology and that expertise is limited. The product differentiation barrier is not of great significance, although it is necessary that a supplier have an established reputation for product reliability. The existence of an adequate and dispersed distribution and service system is also of significance, for the furnishing of efficient on-the-spot assistance in the event of an accident or wheel failure.

Thus, as in the case of antiskid devices, the acquisition of Kelsey-Hayes by Fruehauf is reasonably likely to foreclosure a non *de minimis* segment of the heavy duty wheel market in a market setting in which this should not be allowed to occur.

C. *Potential Competition in Heavy Duty Wheels*

There are two theories under which the elimination of potential competition in a market may be held to violate Section 7: (1) the so-called "actual" potential entrant, and (2) the so-called "perceived" potential entrant. Under the former, an acquisition may be held unlawful if it eliminates the entry into a market of an actual potential competitor, *i.e.*, a firm that, but for the acquisition, would likely have entered the market on either a *de novo* basis or by way of a "toehold" acquisition. Under the latter, an acquisition may be held unlawful if it eliminates a firm which is positioned on the "edge" of a market and is a threat to enter that market, a fact which exerts a procompetitive influence upon the competitive behavior of the companies already in the market. See [111] *U.S.* v. *Falstaff Brewing Corp.*, 410 U.S. 526 (1973); *Ford Motor Co.* v. *U.S.*, 405 U.S. 526 (1972); *F.T.C.* v. *Procter & Gamble Co.*, 386 U.S. 568 (1967); *U.S.* v. *Penn-Olin Chemical Co.*, 378 U.S. 158 (1964); *U.S.* v. *El Paso Natural Gas Co.*, 376 U.S. 651 (1964).

The Supreme Court has fully endorsed the theory of "perceived" potential entry, but has specifically reserved ruling upon the question of violation based upon the "actual" potential entry theory. *U.S.* v. *Falstaff Brewing Corp.*, *supra*, at 537; see also *U.S.* v. *Marine Bancorporation*, 418 U.S. 602, 625, 639 (1974). However, the Commission and lower courts have on a number of occasions embraced this theory of violation, and I take it as binding at the ALJ level. (See decided cases listed in n.23 of the Commission's opinion in *British Oxygen*, 86 F.T.C. at 1361.)

1. Fruehauf as an Actual Potential Entrant

As noted, the heavy duty wheel market is highly concentrated. The procompetitive effect of actual entry on the part of Fruehauf would serve to decrease that concentration. And in determining the question of such entry, guidance should be placed less upon the subjective testimony of respondent's officials, than upon objective factors concerning Fruehauf's capabilities and incentive to enter. *U.S.* v. *Penn-Olin*, *supra*, 378 U.S. at 174.

It is reasonable to infer that, but for its acquisition of Kelsey-Hayes, Fruehauf would have entered into wheel production either now or in the near future. Fruehauf has an established policy of vertical integration; it is in fact the most heavily vertically integrated trailer manufacturer. It manufactures virtually all of the higher cost components for its trailers except for wheels (excluding Kelsey-Hayes production). Fruehauf, [112] like other trailer manufacturers, has been plagued from time to time with shortages of wheels, which have interfered with or curtailed trailer production.

The record demonstrates Fruehauf's efforts to insure a certain source of supply for this vitally needed commodity. To be sure, the company has not attempted *de novo* entry through the conventional cast spoke or disc wheel route. But it has succeeded in developing feasible alternatives, *viz.*, a fabricated aluminum and a fabricated steel heavy duty wheel. After thorough testing, both types of wheels were rated as satisfactory in performance. However, because of somewhat higher costs, both wheel projects were shelved in the early 1970's. But in doing so, Fruehauf was careful to direct that thorough files and records be maintained for resurrection of these projects in the event that rising prices for conventional wheels should permit effective competition. Fruehauf wheels, of course, could be distributed through the same channels used to market other Fruehauf Pro-Par brand products.

The record also demonstrates Fruehauf's interest in encouraging others to enter the heavy duty wheel market. It participated in wheel projects with McConway and Torley and with U.S. Steel. While these programs did not become viable, they do demonstrate Fruehauf's interest in developing sources alternative to existing wheel suppliers. Fruehauf therefore has the interest, incentive and the available means for entry into the heavy duty wheel market when future economic conditions permit.

2. Fruehauf as a Perceived Potential Entrant

To reiterate the findings to some extent, Fruehauf's interest in entering the market was known to the major wheel suppliers. (Zart 1244; Looney 1831; Vause 2204; Mitchell 2592.) Firestone's rim and disc wheel plant was visited in 1971 by Fruehauf personnel [113] "to see how we [Firestone] made rims with the possibility of their [Fruehauf] making their own rims." (Zart 1244.) Dayton-Walther, Fruehauf's principal wheel supplier, was aware that Fruehauf was encouraging the entry of McConway and Torley. (Rupert 802; Mitchell 2542, 2545.) Dayton-Walther has been aware for over ten years that Fruehauf has been working on a fabricated heavy duty wheel design. (Mitchell 2592.) Dayton-Walther believes such a design could be made to perform successfully. (Mitchell 2592.) Prior to its acquisition, Kelsey-Hayes was aware that Fruehauf was working with other companies to develop heavy duty wheels. (Vause 2204.) Webb knew Fruehauf had been interested in a joint venture with Webb to produce heavy duty wheels. Webb viewed Fruehauf's involvement with McConway and Torley as "a venture by Fruehauf to supply wheels for Fruehauf trailers." (Smith 932.) "Fruehauf negotiated an agreement with a contract with McConway and Torley at Pittsburgh to set up McConway and Torley in the wheel business to supply Fruehauf." (Smith 942.) This awareness on the part of wheel suppliers presently in the market together with demonstrated incentives and capabilities of Fruehauf is sufficient to establish that Fruehauf as a perceived potential entrant had a procompetitive "edge" effect on the highly concentrated heavy duty wheel market. *U.S.* v. *Falstaff Brewing Corp., supra,* 410 U.S. at 534-35, n.13; *U.S.* v. *Phillips Petroleum Co., supra,* 367 F. Supp. 1226, 1239 (C.D. Cal. 1973), *aff'd,* 418 U.S. 906 (1974).[39]

D. *Entrenchment in Heavy Duty Wheels and Antiskid*

1. Entrenchment of Fruehauf

As noted, the truck trailer market is highly concentrated, with Fruehauf the leading company by far. Since the mid-1950's Fruehauf's share of this market [114] has stabilized at approximately 25 percent, with its nearest competitor enjoying only half that amount. The remaining companies, with only a few exceptions, have market shares in the neighborhood of 3 percent, 2 percent, 1 percent or less. Fruehauf is already heavily vertically integrated into most major trailer components. Its acquisition of Kelsey-Hayes will permit it to vertically integrate into heavy duty wheels and antiskid devices, both essential components of a trailer (with wheels having been periodically in short supply).

Barriers to entry or to effective, meaningful competition are substantial. Fruehauf, with its full line of trailers, its geographically dispersed plants and almost 100 service centers, and its demonstrated capabilities regarding trade-ins and financing, without Kelsey already enjoys significant advantages over its competitors, major and marginal. Fruehauf's acquisition of Kelsey will permit secure access to the manufacturing and distribution resources of that company, and will serve to further entrench Fruehauf's leadership in the trailer industry and render it that much more difficult for its smaller competitors or prospective entrants to compete or to effect deconcentration.

The Commission and the courts have not hesitated to declare mergers unlawful, where, in an oligopolistic setting, the result of a merger is to confer a competitive advantage on a dominant competitor which creates a reasonable probability of entrenching or increasing that company's market position. *F.T.C.* v. *Procter & Gamble Co.,* 386 U.S. 568 (1967); *General Foods Corp.* v. *F.T.C.,* 386 F.2d 936 (3d Cir. 1967). See legal analysis set forth in *U.S.* v. *ITT Corp.,* 324 F. Supp. 19, 24 (D. Conn. 1970), and in the court's earlier opinion in that case, 306 F. Supp. 766, 775–76 (1969). [115]

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[39] Fruehauf's position as a volume wheel purchaser enabled it (along with other major purchasers) to keep pricing levels down in the heavy duty wheel industry. (Smith 943-44; Rupert 778.) Another beneficial factor regarding present competition in the wheel industry was Fruehauf's efforts to encourage the entrance of additional suppliers.

2. Entrenchment of Kelsey-Hayes

As for Kelsey-Hayes, the record shows that its position in the highly concentrated antiskid and heavy duty wheel markets has been enhanced by its merger with Fruehauf. In antiskid, in 1975 Kelsey-Hayes had a market share of approximately 30 percent. Its nearest competitor had about 20 percent, with the remaining five suppliers having about 10 percent of that market.

It is at least reasonably probable that Fruehauf's established policy of using in-house components will strengthen Kelsey-Hayes' position in the antiskid market by securing Fruehauf's substantial purchases as a captive account for Kelsey-Hayes. This effect is magnified in light of the high economy of scale barrier to entry. The result of removing Fruehauf's substantial purchases from open competition is that the ability of existing competitors to meet the significant economy of scale level and thus, their ability to effectively compete, is injured. Moreover, the economy of scale barrier to entry in antiskid is raised since potential entrants also would have greater difficulty in meeting scale economies without the opportunity to compete for increased volume from Fruehauf's purchases. Moreover, having Fruehauf as a substantial account will assist Kelsey-Hayes in weathering the "shake down" period in this still young industry.

In heavy duty wheels, it is similarly true that the competitive position of Kelsey-Hayes is greatly improved by its prospects of supplying the requirements of Fruehauf. The recently completed $25 million expansion of the Gunite facilities should greatly assist in that endeavor. [116]

Nevertheless, I cannot conclude that Kelsey-Hayes has been "entrenched," as that term has heretofore been used in Section 7 cases. The teaching of *U.S.* v. *ITT, supra,* is that in order to prevail on an entrenchment theory, the government must prove that the acquired company was — prior to the merger — a "dominant" competitor in the relevant market.[40] In heavy duty wheels in 1972 Kelsey-Hayes held a market share of only approximately 15 percent.

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[40] But see *Allis-Chalmers Mfg. Co.* v. *White Consolidated Industries,* 414 F.2d 506 (3d Cir. 1969), *cert. denied,* 396 U.S. 1009 (1970).

This is not dominance. In the antiskid market, as stated above, Kelsey's 1975 market share was approximately 30 percent. But it seems clear to me that Kelsey did not "dominate" that market (although it could conceivably do so in the future with additional Fruehauf purchases). Unlike Fruehauf in the case of trailers, the record does not reveal that Kelsey had "special" advantages over its competitors in manufacturing, selling and distributing its antiskid products.[41] There simply is no record evidence that Kelsey "dominated" the antiskid or the heavy duty wheel market, and violation of Section 7 is not found on that basis.

IX. REMEDY

Complaint counsel have requested the total divestiture of Kelsey-Hayes together with a ten year ban on future acquisitions by Fruehauf of manufacturers and distributors of heavy duty wheels, heavy duty antiskid braking devices and truck trailers.

Total divestiture is considered to be the most effective antitrust remedy and is particularly appropriate in cases of stock acquisitions which are found to violate Section 7. *United States* v. [117] *duPont & Co.*, 366 U.S. 316, 326, 328 (1961); *Ford Motor Co.* v. *United States*, 405 U.S. 562, 573 (1972). Even where the violation relates to but a single aspect of the company acquired, total divestiture is still appropriate in order to reinstitute meaningful competition. *OKC Corp.* v. *F.T.C.*, 455 F.2d 1159, 1163 (10th Cir. 1972).

Moreover, the Commission's power to order a ban on future acquisitions is clear. In recent years, in many instances in which the Commission has ordered substantial divestiture of stock or assets, the order has included a ban on future acquisition in the offending lines of commerce. *Avnet Corporation*, 82 F.T.C. 391 (1973), *aff'd* 511 F.2d 70, 79 (1975), *cert. denied*, 423 U.S. 833 (1976); *Seeburg Corp.*, 75 F.T.C. 561 (1969), *aff'd as modified*, 425 F.2d 124 (6th Cir.), *cert. denied*, 400 U.S. 866 (1970); *American Brake Shoe Co.*, 73 F.T.C. 610 (1968), *aff'd as modified*, 420 F.2d 928, *cert. denied*, 406 U.S. 865 (1970); *Liggett & Myers, Inc.*, 86 F.T.C. 1074 (1976); *RSR Corporation*, 88 F.T.C. 800 (1976).

Respondent suggests that hearings are necessary on the question of relief. To the extent that this constitutes a request that such hearings be scheduled, it is denied, unless so ordered by the Commission.

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[41] I am referring to factors such as, *inter alia*, having a full line of products, geographically dispersed plants and branches, ability to handle trade-ins and financing capability.

X. CONCLUSIONS

1. The Commission has jurisdiction over the subject matter of this proceeding and of respondent Fruehauf.

2. On October 31, 1973, Fruehauf acquired all of the common stock of Kelsey-Hayes. [118]

3. At all times relevant to this proceeding, Fruehauf and Kelsey-Hayes were corporations engaged in commerce, as "commerce" is defined in the Clayton Act, as amended.

4. The effect of the acquisition by Fruehauf of the stock of Kelsey-Hayes may be substantially to lessen competition or to create a monopoly in any line of commerce in any section of the country, in violation of Section 7 of the Clayton Act, as amended (15 U.S.C. 18).

5. The manufacture and sale of the following product lines constitutes a "line of commerce" within the meaning of Section 7 of the amended Clayton Act:

(a) Heavy duty antiskid braking devices;
(b) Truck trailers; and
(c) Heavy duty wheels.

6. The appropriate section of the country within which to test the effect of the acquisition is the United States as a whole.

7. In each of the lines of commerce, prior to the merger, there were high levels of concentration and substantial barriers to entry or to effective competition.

8. In the heavy duty wheel line of commerce, prior to the merger, Fruehauf was one of the few most likely potential entrants.

9. The effect of the acquisition by Fruehauf of Kelsey-Hayes has been or may be to lessen competition substantially or tend to create a monopoly in violation of Section 7 of the Clayton Act, as amended, in the following ways: [119]

(a) actual and potential producers of antiskid braking devices, other than Kelsey-Hayes, have probably been foreclosed from selling to Fruehauf, a substantial purchaser of such antiskid braking devices;

(b) actual and potential producers of heavy duty wheels other than Kelsey-Hayes may be foreclosed from selling to Fruehauf, a substantial purchaser of heavy duty wheels;

(c) Fruehauf's competitors have been or may be foreclosed from a significant source of supply for heavy duty wheels and antiskid braking devices;

(d) Fruehauf has been eliminated as a potential entrant into the manufacture and sale of heavy duty wheels;

(e) Fruehauf's dominant market position will be entrenched by virtue of its secure source for heavy duty wheels and antiskid braking devices; and

(f) barriers to entry in each of the relevant markets have been raised.

10. Divestiture of the acquired stock is both necessary and appropriate to remedy the probable anticompetitive effects of the unlawful acquisition. [120]

XI. ORDER

Accordingly:

I

It is ordered, That respondent, Fruehauf, a corporation, and its officers, directors, agents, representatives, employees, subsidiaries, affiliates, successors and assigns, shall divest all stock, assets, title, properties, interest, rights and privileges, of whatever nature, tangible and intangible, including without limitation all buildings, machinery, equipment, raw material reserves, inventory, customer lists, trade names, trademarks and other property of whatever description acquired by Fruehauf as a result of its acquisition of Kelsey-Hayes together with all additions and improvements to Kelsey-Hayes which have been added to Kelsey-Hayes subsequent to the acquisition. Such divestiture shall be absolute, shall be accomplished no later than six (6) months from the service of the order, and shall be subject to the prior approval of the Federal Trade Commission. [121]

II

It is further ordered, That such divestiture shall be accomplished absolutely to an acquirer approved in advance by the Federal Trade Commission so as to transfer Kelsey-Hayes as a going business and a viable, competitive, independent concern.

III

It is further ordered, That pending any divestiture required by the order, Fruehauf shall not knowingly cause or permit the deterioration of the assets and properties specified in Paragraph I in a manner that impairs the marketability of any such assets and properties. Fruehauf may but shall not be required to make capital expenditures for the improvement of any such assets and properties.

IV

It is further ordered, That pursuant to the requirements of Paragraph I, none of the stock, assets, properties, rights, privileges and interests of whatever nature, tangible or intangible, acquired [122] or added by Fruehauf, shall be divested, directly or indirectly, to anyone who is at the time of the divestiture an officer, director, employee or agent of, or under the control, direction or influence of Fruehauf, or anyone who owns or controls, directly or indirectly, more than one (1) percent of the outstanding shares of the capital stock of Fruehauf or to anyone who is not approved in advance by the Federal Trade Commission.

V

It is further ordered, That for a period of ten (10) years from the date this order becomes final, Fruehauf shall cease and desist from acquiring, or acquiring and holding, directly or indirectly, through subsidiaries or otherwise, without the prior approval of the Federal Trade Commission, the whole or any part of the stock, share capital, assets, any interest in or any interest of, any concern, corporate or noncorporate, engaged in the business of manufacturing, distributing, or selling, heavy duty wheels, heavy duty antiskid [123] braking devices, or truck trailers, nor shall Fruehauf enter into any agreement, understanding or arrangement with any such concern by which Fruehauf obtains the market share, in whole or in part, of such concern in the above-described product lines.

VI

It is further ordered, That on the first anniversary date of the effective date of this order and on each anniversary date thereafter until the expiration of the prohibitions in Paragraph V of the order, Fruehauf shall submit a report in writing to the Federal Trade Commission listing all acquisitions, mergers and agreements to acquire or merge made by Fruehauf; the date of each such acquisition, merger or agreement; the products involved and such additional information as may from time to time be required.

VII

It is further ordered, That within thirty (30) days from the effective date of this order and every sixty (60) days thereafter until it has fully [124] complied with Paragraph I of this order, Fruehauf shall submit a verified report in writing to the Federal Trade Commission setting forth in detail the manner and form in which it intends to comply, is complying or has complied therewith. All such reports shall include, in addition to such other information and documentation as may hereafter be requested, (a) a specification of the steps taken by Fruehauf to make public its desire to divest Kelsey-Hayes, (b) a list of all persons or organizations to whom notice of divestiture has been given, (c) a summary of all discussions and negotiations together with the identity and address of all interested persons or organizations, and (d) copies of all reports, internal memoranda, offers, counteroffers, communications and correspondence concerning said divestiture.

VIII

It is further ordered, That Fruehauf shall notify the Commission at least thirty (30) days prior to any proposed changes which may affect compliance [125] obligations arising out of the order, such as dissolution, assignment or sale resulting in the emergence of successor corporations, and that this order shall be binding on any such successor.

OPINION OF THE COMMISSION

BY DIXON, *Commissioner:*

This case involves a challenge under Section 7 of the Clayton Act to the legality of a merger between the nation's largest manufacturer of truck trailers and a leading maker of automotive components, including two that are needed for the manufacture of truck trailers. The Commission's complaint challenging Fruehauf's 1973 acquisition of Kelsey-Hayes Company was issued on June 21, 1974. A lengthy trial was held before Administrative Law Judge (ALJ) Thomas Howder, who entered an initial decision finding that the merger violated the law and recommended entry of an order requiring divestiture by Fruehauf of Kelsey-Hayes. This matter is before the Commission upon the appeal of respondent from Judge Howder's decision.

Respondent Fruehauf registered sales and rentals of $550.4 million and assets of $556.6 million in 1972, derived principally from the sale, maintenance and service [2] of truck trailers. (I.D. 2-3)[1] Kelsey-

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[1] The following abbreviations are used herein:

I.D.	— Initial Decision (Finding No.)
I.D. p.	— Initial Decision (Page No.)
Tr.	— Transcript of Testimony (Page No.)
CX	— Complaint Counsel's Exhibit No.
RX	— Respondent's Exhibit No.

(Continued)

Hayes for the fiscal year ending August 31, 1972 had net sales of $454.7 million and assets of $243 million. (I.D. 7) Kelsey-Hayes manufactures various component parts for the automotive industry, including automobile wheels, brake drums and drum brake assemblies. It also manufactures heavy duty wheels for use on trucks and truck trailers and in 1975 was the leading supplier of heavy duty *A*nti*S*kid *B*raking *D*evices (hereinafter on occasion for the sake of brevity ASBD) to heavy duty truck, truck tractor, and truck trailer manufacturers. (I.D. 8)

The complaint alleged and Judge Howder found that Fruehauf's acquisition of Kelsey-Hayes had restrained competition in three national markets—heavy duty wheels, antiskid braking devices, and truck trailers. Illegality was premised upon the conclusion that the merger had foreclosed competitors of Kelsey-Hayes from selling to Fruehauf, a substantial purchaser of heavy duty wheels and antiskid braking devices, while foreclosing competitors of Fruehauf [3] from access to a major source of wheels and ASBD. The Judge further found that Fruehauf had been eliminated as a potential entrant into the manufacture and sale of heavy duty wheels, that its dominant position in the truck trailer market had been entrenched by acquisition of a secure source of two components, and that barriers to entry in all three relevant markets had been raised by the acquisition. The ALJ rejected complaint counsel's argument that cast spoke truck trailer wheels (exclusive of rims) constituted a relevant submarket within which to test effects of the merger, and further rejected the suggestion that an unlawful effect of the merger had been to entrench Kelsey-Hayes in any relevant markets. These contentions have not been pursued on appeal.

While most of the judge's findings of fact are not contested, respondent quarrels with the ALJ's interpretation of those facts and his ultimate conclusions, and complaint counsel urge that we modify and augment various factual findings. We believe the initial decision reflects a conscientious attempt to resolve the issues presented by a massive trial record, but based upon our own review of this record and of the contentions of the parties on appeal we have modified certain findings and conclusions of the ALJ, as will shortly appear.

CPF — Complaint Counsel's Proposed Finding of Fact at Trial Before the ALJ (No.)

RPF — Respondent's Proposed Finding of Fact (No.)

RAB — Respondent's Appeal Brief Before the Commission (Page No.)

CAB — Complaint Counsel's Answer Brief Before the Commission

GENERAL OBSERVATIONS

We count it our blessing that there is essentially no disagreement between the parties at this stage of the proceeding over the relevant markets in which the effects of this merger are to be judged, they being the nationwide markets for heavy duty wheels, antiskid braking devices, and truck trailers. To compensate there is ferocious dispute as to the way in which the Commission should go about answering the ultimate question in this case, whether the effect of the challenged acquisition in any of the relevant markets "may be substantially to lessen competition. . . ."

Respondent argues that the query may be recharacterized as "will the merger maintain or enhance, in any line of commerce, 'market power', i.e., the ability to maintain a serious and persistent monopolistic deviation of price from cost." (RPF 4, 16) Such market power in respondent's [4] view can exist only in a market environment in which there are (1) sufficiently few sellers that all recognize their joint interest in pursuing coordinated pricing strategy, and (2) sufficiently high barriers to entry to insulate firms in the market from the competitive pressure of potential entrants. [Tr. 5664, 6807, 6829]

Respondent contends, therefore, that illegality from the vertical effects of a merger may be found only in the presence of *both* high market concentration (whose existence in at least some of the markets involved here is not challenged) *and* high barriers to entry (existence of which is the subject of vigorous disagreement).

Not surprisingly, much of the lengthy trial record in this case is devoted to an assessment of the barriers to entry into the relevant markets. Drawing on the line of analysis elaborated by Professor Joe Bain in *Barriers to New Competition*, the parties have defined these barriers to include (1) capital costs[2] (2) absolute costs[3] (3) economies of scale[4] and (4) product differentiation[5].

[5] Before accepting this schema we believe that several important

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[2] The amount of money needed to build and equip a production facility of minimum efficient size, including inventory, working capital, (and research and development, see n. 19 infra.) I.D. 32.

[3] Advantages, such as patents, which impose upon new entrants a cost penalty such that the entrant would have a higher unit cost at the same level of output as existing firms. I.D. 37.

[4] The level of output or market share that a prospective entrant would need to achieve so as not to be at a unit cost disadvantage compared to existing competitors. I.D. 38. Where economies of scale are high (which some economists define as 10 percent or more, *i.e.*, a firm needs 10 percent or more of the market to produce at minimum unit cost) entry will prove more difficult, because the entrant must either wrest significant market share from other firms or significantly expand industry output, either of which endeavors is likely to depress price, perhaps to a point at which the potential entrant will decide that it does not desire to enter after all. Lesser economies of scale may raise formidable barriers for the same reason.

[5] The barrier existing when a new entrant must charge lower prices or spend extensively on sales promotion in order to divert buyer loyalties from an established seller, I.D. 41, (because buyers perceive differences in essentially fungible products.)

qualifications are in order. The analysis of barriers to entry in antitrust is useful only insofar as it provides a measure of the difficulty which potential competitors will experience upon seeking to enter a market in the event that firms already in the market should happen to set prices at supra-competitive levels. In a market with high barriers to entry, market participants will presumably enjoy great leeway to depart from competitive norms without having to face the restraining force of new entry. Conversely, it is argued that even in a highly concentrated industry, if entry barriers are low, there is little danger of market abuse because such abuse will quickly elicit new entry to restore prices to competitive levels.

But these are not "either/or," "all or nothing" propositions and we expressly reject the notion that they are. Barriers to entry may be arrayed along a continuum from high to low, measuring the difficulty which outsiders will experience in becoming insiders and conversely the ease and safety with which insiders may raise prices without fear of outsiders. It does not make sense, we think, to assume that there exists some magic dividing line between "high" and "low" barriers such that industries on one side are immune to anticompetitive infection by vertical mergers while industries on the other side are able to offer no resistance.[6] Rather, the magnitude of barriers to entry is only one factor to be weighed in any assessment of the likely effects of a merger. The presence of lower barriers to entry may serve to moderate the anticompetitive effects of a merger or ensure that they are shorter lived, but it will not necessarily ensure that such effects do not arise. This point, which has great force in the analysis of horizontal mergers, *e.g., RSR Corp.,* 88 F.T.C. 800, 899 (1976); *Ekco Products Co.,* 65 F.T.C. 1163, 1208 (1965), *aff'd.* 347 F. 2d 745 (7th Cir. 1965); *Jim Walter, Inc.,* Dkt. 8959 slip op. p. 46 (December 20, 1977) [90 F.T.C. 671 at 730], is not wholly irrelevant with respect to vertical [6] acquisitions. Determination of whether a vertical merger is likely substantially to lessen competition should depend upon an analysis of the interaction of various factors. That barriers to entry do not attain some necessarily arbitrary level called "high" should not, as it were, "foreclose" further analysis.

A closely related point is that high concentration, (and the opportunities for interdependent conduct that accompany it) may itself constitute a barrier or deterrent to entry. If the number of firms in an industry is sufficiently small that they are able to act in tacit concert to *raise* prices, why should they also not be able to act in similar fashion to *lower* prices predatorily in the face of a competitive threat from a new entrant? Recognition of this possibility may deter outsiders from attempting entry into a concentrated industry notwithstanding that other barriers, such as the costs of necessary capital, are low. In turn, industry members are spared the necessity to make good on their implicit threat to discipline new entrants, and prices remain at supra-competitive levels. It follows from this that a merger, simply by enhancing concentration in an industry[7], may also enhance the barriers to entry into it, or the market power of its members, notwithstanding that other barriers to entry remain low.[8]

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[6] Professor Bain himself makes this rather obvious point, *e.g.,* Bain, *supra,* pp. 4-5, 203-204, and we do not mean to imply that respondent is not fully cognizant of it (*e.g.* RPF 42). But occasionally the point gets lost in the argument, where it is suggested that the absence of "high" entry barriers precludes any exercise of market power or finding of anticompetitive effects.

[7] In similar fashion, vertical integration itself may constitute, or enhance a barrier to entry, by restricting the outlets to which a prospective entrant may be able to turn (or will view itself as able to turn) if it attempts to compete.[9] For example, if a firm needs 20 percent of a market in order to realize an acceptable profit on its investment, and if 20 percent of the market comes under control of various suppliers through purchase of customers, the potential entrant may be viewed as needed 25 percent (20/80) of the remaining market in order to enter. Mergers between customers and suppliers thus serve to make it more difficult for would-be competitors of the supplier to enter.[10]

[8] In sum, no matter what the extent of barriers to entry into a highly concentrated industry, a merger between a major customer and a major supplier may restrain competition in the market for the *supplier's product* (in the case before us ASBD and heavy-duty wheels) by foreclosing competitors of the supplier from the possible patronage of the customer and thereby (1) increasing the market share of the leading firm, increasing industry concentration, and thus enhancing the industry's capacity to act in concert; (2)

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[7] Whether a vertical merger will actually heighten concentration within an industry is, of course, problematical. It may well have such an effect by diverting the patronage of the merging customer to the merging supplier where such supplier might not otherwise have obtained it. Where such patronage is diverted from the smaller members of the industry, to those with dominant market position, the result may be to enhance concentration.

[8] Professor Bain himself addresses this point, *Barriers to New Competition*, pp. 94ff though with what resolution is unclear. There are obviously other possible scenarios in which a concentrated industry might not respond to new entry by seeking to keep out the entrant. See generally, Scherer, *Industrial Market Structure and Economic Performance*, pp. 219 ff.

[9] The *necessity* for vertical integration, by increasing the necessary cost of capital, is recognized as a barrier to entry under the rubric of capital costs. We refer to a slightly different effect.

[10] Respondent suggests, and some economists argue, that it would be irrational for a customer to favor in-house supplies over less costly outside sources, so that a new entrant offering a cheaper product should not be deterred by its competitors' ownership of the new entrant's potential customers. In this case there is evidence that respondent favored in-house procurement, even where outside procurement might be cheaper. (I.D. 51) Moreover, it seems hardly unreasonable to postulate that given rough equality of offerings, the in-house supply will be favored, as it might where the desire is to deter or discipline a new entrant. Moreover, the *expectation* that captive customers will not bestow their patronage nondiscriminatorily upon outsiders (whether well-founded or not in a particular case) is what operates as the deterrent. That expectation is well illustrated in this record as well. (*e.g.*, I.D. 50)

rendering more difficult continued market participation by smaller firms which may depend on the possible patronage of the foreclosed customer to remain in the market; or (3) rendering more difficult, and thus less likely, entry by other firms which are discouraged by the diminished opportunity to secure patronage of the foreclosed customer.[11]

With the foregoing qualifications in mind we proceed to consider the particular markets in which anticompetitive effects of this merger are alleged. [9]

HEAVY DUTY ANTISKID BRAKING DEVICE MARKET

An antiskid braking device is safety equipment installed on the braking systems of air-braked vehicles to monitor and if necessary override the driver's action during braking to prevent wheel lock-up and possible skidding. (I.D. 11) ASBD consists principally of three matched components: a sensor which determines the speed at which a wheel is rotating; a computer or logic module which calculates the speed at which the wheel should rotate in order to achieve maximum braking efficiency; and a valve which regulates the air pressure so as to release the brakes momentarily in the event of an impending skid. (I.D. 11)

Development of the antiskid braking device was largely the result of Federal Motor Vehicle Safety Standard (FMVSS) 121 (49 C.F.R. 571.121, as amended), promulgated by the National Highway Traffic Safety Administration of the United States Department of Transportation. Although the performance standard does not specify the use of ASBD, the device is the only product presently available which satisfies the standard. (I.D. 12) The standard required ASBD for most heavy-duty air-braked truck trailers manufactured after January 1 and air-braked trucks and truck tractors manufactured after March 1, 1975. The market is accordingly a young one whose future, however, enjoys a measure of governmental support. (I.D. 15)

As the ALJ observed, concentration in the manufacture and sale of

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[11] Compare two highly concentrated industries, in one of which barriers to entry are of sufficient height that industry members are able to raise prices 25 percent above competitive levels without attracting new entry, in the other of which firms can depart by only 2 percent from competitive levels before new entry is called forth. A vertical merger in the first industry would substantially lessen competition if it raised barriers even further and enhanced market power so that industry members could now raise prices by, say, 28 percent before attracting entry. But the *same* substantial lessening of competition would be done in the low-barrier industry if a vertical merger raised those low barriers so that firms were able to depart by 5 percent (instead of the former 2) from competitive levels before facing a threat from outside. (Needless to say, the state of economic learning does not permit, nor does the Clayton Act require, probable effects of mergers to be measured with such precision.)

Again, we do not suggest that respondent's able counsel are unaware of this point: "If they [entry barriers] are low *and are not increased by reason of the merger*, then there is no market power conferred upon the acquiring company; and, in the absence of market power, Your Honor, there is no probability of a substantial injury to competition." (Tr. 7, emphasis added).

ASBD is very high. Only seven companies competed in the market in 1975 and 1976, with the top two firms accounting for over 50 percent of total 1975 unit sales, and the top four firms carrying off 74 percent of the business. (I.D. 16) The leading firm in the market, Kelsey-Hayes sold 32.5 percent of all ASBD units and took in 28.6 percent of total dollar volume. Fruehauf's 1975 purchases of ASBD units were $1,938,614, or 4.7 percent of the dollar universe and 5.4 percent of unit volume. (I.D. 46, Tr. 6530 *in camera*) Because FMVSS 121 was modified to eliminate antiskid devices on the front axles of trucks and truck tractors, it is likely that in years after 1975 Fruehauf's purchases of ASBD did and will constitute a significantly larger percentage than 4.7 or 5.4 because Fruehauf manufactures only trailers, whose need for ASBD has not been changed. (I.D. 47; Tr. 6534 *in camera*) [10]

Capital Costs and Scale Economies

Judge Howder further concluded that barriers to entry into the ASBD market are significant. His conclusion as to entry barriers is based principally on evidence of moderately high[12] capital costs, ranging up to 13 to 14.6 million dollars for some initial entrants and high scale economy requirements. (I.D. p. 108) Respondent notes in reply that the ASBD market is in a state of flux and that a trend may be discerned toward standardization and simplification of the three braking components which at some unspecified future time may permit entry on a less costly basis than that which occurred initially. Respondent further contends that even firms which might enter now on a "systems" basis will likely be able to do so without incurring the same magnitude of research and development costs experienced by the pioneers, (I.D. 35) and that evidence of scale economies cited by the ALJ is inapposite because it is based merely on assessments by industry members of market shares needed to realize a satisfactory rate of return on existing plants, not on the hypothetically most efficient plant which a new entrant might be able to build.

On balance we believe that the ALJ's conclusions with respect to the significant barrier created by capital costs and scale economies in this market are correct. The market for antiskid braking devices is not a large one. Sales of the product in 1975 measured approximately $41 million. (I.D. 46, CX 612A-B *in camera*) Sales may well have declined in later years because of the previously noted change in FMVSS, eliminating the need for ASBD on the front axles of trucks and truck tractors. (I.D. 47)[13] Given a market size [11] of $40–$50 million, capital costs in the vicinity of $8–$10 million obviously loom exceedingly large.[14] It is no wonder that industry witnesses testified that their companies hoped, expected, anticipated, and *needed* to capture 20 percent or more of the market in order to reap a satisfactory return on their investments. (I.D. 39; Tr. 2606–07 *in camera*, 1144, 2450 *in camera*, 1017–18)

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[12] At I.D. p. 108 the judge refers to "high to moderate," *i.e.*, from several million dollars to $14.6 million. Opposing expert witnesses classified these barriers as "moderate" and "on the borderline between moderate and large." (I.D. 34)

Nor is it clear that this situation is likely to change appreciably for would-be second generation entrants, if there are any. While future entrants may be able to improve upon the $13 and $14.6 million capital costs experienced by certain of the pioneers, the record nevertheless reflects costs faced by the earliest entrants that future potential competitors will be unable to avoid, for example, the costs of tooling, machinery and related facilities, and necessary [12] inventory, which alone have aggregated nearly $5 million for some cases. (Tr. 1015; cf. 2444–45)[15] Moreover, while *some* diminution of research and development costs may be effected by second-generation entrants, it is likely that firms entering today will face additional costs, including the burden of paying Original Equipment Manufacturers (OEM's) to test and obtain certification for their product, in contrast to the situation facing initial entrants where OEM's, under the pressure of impending federal requirements, shared and often paid in full the costs of product certification testing. (CX 83, 99, 199C; RX 89; Tr. 1699, 2213, 2459–60 *in camera*, 2475 *in camera*, 2603, 2611, 5853)

For these reasons, then, we think that an estimate of capital barriers approaching $8–$10 million for some new entrants would not be unreasonable, and given the small size of this industry, even a capital barrier half that amount would pose a formidable impediment to any firm whose goals in entering are other than philanthropic.[16]

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[13] A factor tending to *increase* the estimate of market size is that not until March 1, 1975 was ASBD required on trucks and truck tractors, as noted above. Elimination of the front-axle requirement, however, would seem to more than offset this factor in terms of expected demand for post-trial years.

[14] We are not attempting here to obscure Professor Bain's distinction between the "absolute capital requirement effect" and the "percentage effect" of scale economies on the condition of entry. Bain, *supra*, p. 55. As Bain notes, the absolute amount of capital required for entry may be significant because it is so large that relatively few individuals or groups could secure it. [We would modify this observation by noting that the absolute amount of capital required for entry is also important as a rough measure of the *risk* faced by a new entrant. Even where a firm is able to raise a certain sum, it may be reluctant to *risk* that money in an untried market. That is why capital costs of $10 million pose a greater barrier to entry than costs of $5 million, even though as a practical matter there may be many firms capable of raising either amount. That is also why we reject the suggestion at p. 16 of Respondent's Appeal Brief that even $100 million is not a serious obstacle to firms with access to the money markets.]

On the other hand, even where the amount of capital needed to enter is within the reach of many firms, it may be so large in relation to the size of the market that it can only be invested profitably if the firm is able to secure a large share of the market. While $10 million may be a "moderate" impediment in absolute terms, it is clearly an enormous barrier when matched against a potential market of only $40–50 million in sales.

[15] The comparable figure for Kelsey-Hayes exceeds $3.1 million. (CX 43, CX 242L *in camera;* CX 248B)

[13] Respondent urges that we acknowledge the newness of this industry (which we do), gaze into our crystal ball, and foretell the day when the industry, rather than consisting of sellers of systems, will consist of a larger number of sellers of the components of ASBD (principally the sensor, logic, and valve) all having entered at minimal cost. On the basis of the record before us we believe such a prediction is unwarranted. While it is clear that some standardization of the sensor (which accounts for 15-30 percent of the price of ASBD, Tr. 716, 1126, 1294, 2648, 4341 all *in camera*) has occurred (I.D. 22) a similar result for the logic and valve is less easy to discern.[17] The market involved here is one of *systems* manufacturers which sell to manufacturers of trucks, truck trailers, and truck tractors. Some systems manufacturers may purchase various components from one or more suppliers, but these suppliers cannot realistically be regarded as potential market entrants for reasons detailed by the ALJ at I.D. 57-59.[18] If forced [14] to make a prediction about this market, we think it more likely that the future will find it even more concentrated than it is already, as some of the seven firms already present conclude that they cannot realize the profit most seem to feel they need to reap an adequate return on their investments. (Cf. Tr. 2222)

Respondent argues that testimony by industry members regarding "breakeven" points is not probative of the existence of high scale economies. In essence it is respondent's position, as amplified by its expert witness at Tr. 7541 ff. that merely because all the existing members of the industry have chosen to enter with capital investments that require capture of 15 percent, 20 percent, 25 percent or more of the market to realize an adequate rate of return does not prove that some new firm could not produce ASBD equally as cheaply with a smaller capital investment that required only a tiny fraction of the market to make the investment profitable.[19]

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[16] The record also reflects a substantial *time* component to entry. It has taken many firms four or more years to develop an ASBD and prepare to market it. (CX 190B, 191Q, 194B, 556B, Tr. 442, 1027, 1069-70, 1077, 1080-81, 1105, 1670-71, 2444 *in camera*, 5849) although evidence also indicates that one entrant was able to effect entry in a shorter period (Tr. 669, 727-31, late 1971 to mid. 1974). The time required for entry is obviously a barrier because the greater the time needed for entry, the more likely it is that the market conditions which make entry attractive will change.

[17] There is presently little interchangeability of logic modules and valves between ASBD producers (Tr. 1080, *but see* Tr. 4179, 4181 *in camera*) and the economic incentives to standardize or make interchangeable logics and valves are apparently less than those existing for wheel end hardware. (Tr. 2452-53) Some manufacturers combine the logic and valve into a single unit, which is thought to simplify installation by OEM's, although opinions differ as to whether this matters. (*e.g.*, Tr. 692 *in camera*, Tr. 2672-73; see also I.D. 24) Moreover, the desire for single source responsibility militates against a components market. (I.D. 27) Standardization of the sensor alone apparently does not vitiate this consideration. (Tr. 1025-26)

[18] Moreover, even on a components basis, the record indicates substantial scale economies that would tend to discourage entry. (*e.g.*, Tr. 4384 *in camera*, 4318) With respect to logic modules, one manufacturer was able to grant a per-unit price concession of 10 percent as volume was increased from 30,000 to 100,000 units. (Tr. 4296-7, 4318) In the case of valves, testimony indicated that at least 50,000 units of production might be needed to allow entry at costs comparable to existing competitors. (Tr. 4377 *in camera*) 50,000 units would represent nearly 13 percent of the 1975 unit universe. Complaint counsel suggest a figure of 72,000; but the witness stated "you could probably go as low as 50,000. . ." Tr. 4377. While existing competitors may not be producing at minimum efficient cost, they are surely (by definition) not producing *below* it; hence the 50,000 figure, if anything, understates the volume needed to achieve minimum efficient scale. (*See* CPF 73; *Respondent's In Camera Reply to Complaint Counsel's Proposed Findings*, p. 1).

[15] We agree that as a theoretical proposition the percentage of a market which an existing plant requires to "break even" is not necessarily indicative of that percentage of the market which a new entrant would need to capture in order to enter at the minimum efficient scale, because the existing plant may be larger than necessary to operate at minimum efficient scale. But merely because the testimony of industry witnesses is not as valuable as a more detailed economic analysis (of the sort that neither side has proferred and the industry's youth probably precludes) is, we believe, no reason to disregard such testimony in this case.

Each of the firms which entered this market presumably had to make a judgment as to the level of investment necessary to permit production at the lowest possible cost. While it is understandable that a firm may choose to enter an industry with greater capacity than needed to ensure minimum cost production (because the firm desires a larger market share and larger profits[20]) we must presume that the decision to enter reflects some balancing of risks against competitive necessities. A firm may not confine itself to the minimum efficient plant size, but neither would it seem likely to make an *initial* investment in an *untried* industry that is grossly in excess of what it believes necessary to compete on an equal footing with other industry members. Each of the firms now competing in ASBD was, only a short time ago, in the position of entering *de novo* into ASBD. One firm, whose representatives testified, had failed to make successful entry after substantial expenditures (Tr. 2444). Each of the witnesses testifying with regard to scale economies expressed their belief that scale economies are high, as reflected by the fact that a large percentage of the market was deemed necessary to permit their firms to enter the market or to remain in it once having entered. (I.D. 39) Allowing, as we do, for some exaggeration, uncertainty, and imprecision in the estimates of these witnesses, (who gave figures ranging from 16 percent to 50 percent) we nevertheless believe it is correct to conclude that scale economies in this small market are "high" (*i.e.*, 10 percent or more) and that firms are not likely to contemplate entry in the foreseeable future [16] except on the supposition that they must capture 10 percent or more of this market to get in. This is obviously a formidable barrier to entry because, as acknowledged by both sides, where a firm needs a substantial share of the market to enter profitably and efficiently, the struggle to obtain such a share can be anticipated to reduce prices below the level which attracts entry in the first place. (see n. 4 *supra*)

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[19] Respondent also objects to the seeming inclusion by industry witnesses of research and development expenses as part of necessary investment when estimating what market share they needed to break even. RB 21. The experts disagree on the relevance of R&D expenditures in the measurement of economies of scale. (Compare Tr. 7562–64 with Tr. 7264.) In our view R&D is relevant in estimating economies of scale to the extent that a new firm may have to invest in R&D in order to enter on an efficient basis. Because R&D expenses may be slightly lower for second-generation entrants in this industry is some reason for assuming that efficient entry may be possible at a lower cost in the future, just as added certification costs (see p. 12 *supra.*) may increase the necessary minimum investment.

[20] In this regard it also appears that the original entrants may have overestimated the likely size of the market, *e.g.*, CX 244D, Tr. 2208 *in camera;* 2220.

Product Differentiation Barrier

We think the ALJ's conclusions with respect to the effects of product differentiation in this market are well-balanced and properly reflect the record, although we would amplify them in a few respects. Product differentiation is generally less significant in the case of producer goods than it is for some consumer goods. (I.D. 41) Nevertheless, given the safety-related character of the product in question, the record suggests that firms are at an advantage if they have a reputation for high quality and reliability, both with respect to other automotive components and with respect to ASBD. In part because ASBD is a safety-related item, purchasers have shown reluctance to try any new supplier for fear of new problems and major consequences if failures occur. (Tr. 561-62, 1082-83, 1181, 2611-12, 4359 *in camera*) Reluctance to switch suppliers also stems from the long lead time required to engineer a given ASBD system into a truck tractor. (Tr. 1180-81) For these reasons it is likely that a new entrant would find itself at a modest disadvantage compared to existing competitors, necessitating some additional promotional expenditures.[21] While this barrier is, as Judge Howder concluded, hardly "insurmountable" it is cause for concern, particularly in combination with the more significant barrier posed by capital costs and scale economies. [17]

In light of the considerations above we believe that the ALJ's characterization of the competitive climate in ASBD as "sufficiently unhealthy" (I.D. p. 109) to warrant condemnation of the merger is apt. The effect of this merger will most likely be to remove from the competitive reach of potential entrants into the ASBD market (or existing fringe competitors in the ASBD market) the possible patronage of a major purchaser whose business may be necessary to permit entry into, (or survival in) the market by such firms. One would not, of course, necessarily expect the full effects of this merger to be felt while the trial of the case is pending, since whether or to what extent the respondent chooses to patronize Kelsey-Hayes is a matter solely within its own control. Nevertheless, even such evidence on this point as now exists suggests cause for concern. As Judge Howder found, Fruehauf purchases roughly half of its ASBD requirements from Kelsey-Hayes, a development that appears to have surprised some industry observers. As of August 1973, shortly before the merger, competitors of Kelsey-Hayes did not consider it a likely candidate to become a standard supplier of ASBD to Fruehauf, due primarily to its lack of an in-axle sensor design. As of that August, shortly before the merger, Kelsey-Hayes was not and knew it was not an approved ASBD supplier to Fruehauf because of its lack of such a sensor. (I.D. 49) Because of Fruehauf's acquisition of Kelsey-Hayes in October 1973, the latter's competitors believed that it would get at least a part of Fruehauf's patronage, particularly given Fruehauf's well-recognized policy of buying in-house, notwithstanding that it may sometimes be more economical to purchase from outside sources. (I.D. 50–51) In fact, Fruehauf eventually selected Kelsey-Hayes to supply ASBD for its dry freight vans, comprising 50 percent of production. (I.D. 53)

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[21] Each current ASBD producer spent "a lot of money" on advertising through direct mail and brochures so as to enhance their reputation with the OEM's and their fleet customers. (Tr. 2220-21) Such advertising stressed the firms' reputation in ASBD related fields as well as their reputations in the heavy duty vehicle field. (CX 47C, 190B, 191P-Q, 198N, 199C, 200, 201, 550G)

The reaction of one participant in this market, a competitor with a small market share, regarding the effects of the merger upon his company was as follows:

> . . .we thought we had an opportunity for half the business at Fruehauf, which we no longer have. Beyond that, we would have smaller volume, and as I mentioned earlier, the business is volume sensitive. It would have some impact, and I have not calculated the amount, but some impact on our cost. (Tr. 1153)

[18] Now it is not the role of the Federal Trade Commission to determine from whom Fruehauf Corporation should purchase the components for its truck trailers. It is to be hoped that it will make such decisions upon the basis of which supplier offers it the best product for the lowest cost, thereby inducing all suppliers to strive to improve their products and lower their costs. A major difficulty with vertical mergers, however, is that they make it less likely with respect to the merging customer that this process will occur, because the incentive of other firms to compete for the patronage of the

merged customer is diminished and this incentive may be the one that is needed to ensure entry into a market or continued participation in it by a small firm.[22]

In this highly concentrated industry, given the difficulty of entry and the necessity for firms to capture significant market share in order to compete, we believe that the acquisition by a major customer of the largest firm in the market can only serve as a substantial deterrent to competition and a solidifier of existing market power, by (1) enhancing the market share of the largest firm, (2) increasing already significant barriers to entry, and (3) making more difficult continued participation in the market by firms with smaller market shares. For each of these reasons we believe that Judge Howder correctly found that the merger is likely substantially to lessen competition in the market for heavy duty antiskid braking devices. [19]

Precedent in this area is not inconsistent with our conclusion. As respondent observes, there are no *per se* rules with regard to vertical mergers, and each one must be judged in light of existing market conditions. For this reason prior cases involving different markets and different market conditions give at best imperfect guidance.[23] We would, however, observe that the degree of vertical foreclosure threatened by this merger in ASBD, 4.7 percent of dollar volume and 5.4 percent of unit volume in 1975 and most likely somewhat more in later years (p. 9 *supra.*) is hardly *de minimis* and exceeds the amounts of foreclosure found in vertical mergers that have been previously condemned, *e.g., Brown Shoe Co.* v. *United States,* 370 U.S. 294 (1962); *Ash Grove Cement v. FTC,* 85 F.T.C. 1123, 1164–65 (1975); *United States* v. *Kimberly Clark,* 264 F. Supp. 439, 462–3 (N.D. Cal. 1967). Moreover, while this case does not involve certain of the conditions which troubled the Court in *Brown Shoe,* in other respects it presents greater cause for alarm, because the industry in which this merger's harmful effects are predicated is much more concentrated and difficult to enter than those involved in *Brown Shoe.*

Respondent highlights the fact that in *Brown Shoe* a major purpose of the merger was to force the acquirer's product upon the acquired customer, whereas here the acquisition was purportedly intended purely as a business investment. The purpose of a vertical merger, to the extent that it can be reliably discerned (and quite often it cannot be) may be of some assistance in predicting the merger's probable effect. But where the asserted purpose of a merger is benign, it must take a back seat to more objective evidence of what is likely to result. [20]

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[22] In this regard it should be noted that a major segment of the ASBD market is already foreclosed to competitors because General Motors is largely supplied by its subsidiary AC. (I.D. 54) It is also noteworthy that no claim is made that this merger will promote greater efficiency and lower costs in the production of ASBD or in any of the other markets involved. Thus, one oft-proclaimed justification for vertical integration is not present here.

[23] This observation applies with equal force to the Department of Justice "Merger Guidelines," 1 CCH Trade Reg. Rep. ¶4510 at 6881. These Guidelines indicate that the Department will ordinarily challenge vertical mergers in which the supplying firm accounts for more than 10 percent of its market (here Kelsey-Hayes accounts for about 30 percent) and the acquiring firm accounts for more than 6 percent of purchases (here Fruehauf accounts for 4.7 percent of dollar volume purchases and 5.4 percent of unit volume in 1975, and probably more thereafter). These Guidelines are merely a public statement of intended allocation of prosecutorial resources; where the relevant statistics depart slightly in either direction we fail to see how the Guidelines can be of much comfort to either side in the face of a full record.

Moreover, while a major reason for Fruehauf's acquisition of Kelsey-Hayes was arguably Kelsey-Hayes' perceived value as an investment, the opportunities for strengthening Kelsey's position in at least one relevant market were not lost on Fruehauf management. An August 16, 1973 memorandum to the Fruehauf Board of Directors cited as one advantage of the merger that:

> . . .making the Kelsey unit standard on our trailers will have a beneficial effect on Kelsey's sales of anti-skid control systems to other trailer manufacturers. . . . CX 244D.

This is, of course, precisely the effect that Section 7 was intended to prevent. There is a great advantage in the ASBD market, as we have observed, in having experience and reputation, and being supplier to the nation's largest truck trailer manufacturer is obviously an important selling point for any ASBD producer. But whether or not a firm is entitled to claim this selling point should depend upon whether it offers Fruehauf the best bargain, and not upon whether it is in Fruehauf's interest to bestow patronage upon the firm because Fruehauf owns it.

We hasten to add our acknowledgment that the reasons offered by a subordinate for taking action cannot necessarily be cited as reasons for the action, but clearly Fruehauf did not undertake this merger unaware that it might yield certain anticompetitive results. For this reason as well we are unpersuaded that evidence of other, competitively neutral motivations for the merger should lead us to discount solid record evidence of its probable substantial anticompetitive effects. [21]

HEAVY DUTY WHEEL MARKET

A heavy duty wheel consists of a hub, a center member, and a brake drum. (I.D. 153) There are basically two types of heavy-duty wheels, (1) cast spoke and (2) disc, which are not freely interchangeable on the same axle or vehicle and are not even generally found in the same fleet. (I.D. 155) Nevertheless, both types of wheels compete for direct sales to vehicle producers and for indirect sales to ultimate users. (I.D. 161)

The *cast spoke wheel* consists of a center member (called a "spider") with an integral hub, plus a brake drum and a demountable rim. The spider (with hub) and drum are usually sold assembled together. Rims are usually purchased separately and attached to the wheel and drum assembly by the OEM. (I.D. 157)

The *disc wheel* consists of a center member (called, unsurprisingly, a "disc") with an attached rim, plus a brake drum and a hub. The OEM generally purchases the hub and brake drum assembly separately and attaches it to the disc (with attached rim). (I.D. 158–159) A heavy duty cast spoke wheel (which includes a hub) plus two rims, performs the same basic function as two heavy duty disc wheels (which include rims) plus a hub. (I.D. 159)

The major sellers of heavy duty wheels generally produce either the spider for the cast spoke wheel or the disc for the disc wheel. Each of the spider producers (Dayton-Walther, Kelsey-Hayes, Webb, and Erie) also manufactures heavy duty drums, and all but the smallest, Erie, also make hubs. (I.D. 165–66) Similarly, the disc producers (Firestone, Budd, Motor Wheel, Kelsey-Hayes, Alcoa) with one exception (Alcoa) also manufacture the attached rims. Three of the five disc producers also make heavy duty drums and hubs. (I.D. 167, 169) Firestone, Motor Wheel, and Budd dominate the production of discs, while Kelsey-Hayes produces discs for the lighter end of the market, 14,000–26,000 tons Gross Vehicle Weight. (I.D. 169, 171) [22]

As the foregoing suggests, the key components of a wheel assembly may well be manufactured by different companies. Moreover, some OEMs purchase all heavy duty wheel components separately. (I.D. 163) As a result, there are some companies which do not produce a center member (spider or disc), or sell a complete wheel assembly, which may nonetheless be considered as being in the wheel market by virtue of their production of heavy duty hubs or brake drums.[24] (I.D. 173 ff; I.D. p. 63) However, as noted above, the major factors in the industry are those firms which manufacture the center member as well as other components. (I.D. 165) Four of these firms, Firestone (disc), Dayton-Walther (cast), Kelsey-Hayes (principally cast) and Budd Co. (disc) accounted for 69.52 percent of dollar volume of sales in 1972, and two others, Motor Wheel and Webb, together with Rockwell and Reyco (which do not manufacture the center member) brought the market share of the top eight firms to 93.05 percent. (I.D. p. 64)

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[24] Three axle producers, for example, make both hubs and drums which may be sold attached to the axle. (I.D. 173)

Successful new entry into the heavy duty wheel market appears to be an uncommon occurrence. The existing spider manufacturers have been in the market for many years, with Webb (entry 1946) the most "recent" entrant among existing manufacturers. (I.D. 248) No witness could identify any significant entry into the production of discs for heavy duty disc wheels or heavy duty rims within the last ten years. (I.D. 249) Similarly, nearly all producers of heavy duty drums are longstanding market participants. Entry into heavy duty brake drums and hubs in the last ten years has been confined, with one exception, to diversification by producers of other finished heavy duty wheel components. (I.D. 251)

Respondent generally ascribes this situation to the stellar performance of the market, arguing that entrants have been discouraged by the low rates of return achieved by existing competitors which are under "tight competitive pressure." Complaint counsel contend to the contrary, that profits are above normal, and that the absence of new entry [23] may be ascribed rather to significant entry barriers.[25]

Much of the disagreement in the briefs regarding the magnitude of barriers to entry into the heavy duty wheel market appears to stem from disagreement over how "entry" should be defined. It is clear that "entry" on a level approaching that of the industry leaders is not a simple matter, and barriers thereto are significant. Entry at more modest levels, that may be insufficient to challenge the dominance of industry leaders, is correspondingly easier.

The most detailed record evidence regarding costs of entry into cast wheels was provided by respondent's expert witness on foundries, Mr. Joseph Greenberg. He prepared a study estimating costs of entry for production of spiders and drums at four different levels of plant addition and at various levels of production, ranging from 50,000 to 300,000 units per year. Mr. Greenberg's study indicates first of all that unit costs of production decline at least up to levels of 300,000 units, (CX 280A-F; CX 281J, O) which constitutes 8.9 percent of average heavy duty wheel production for the years 1972-74. His study further indicates that entry via production of cast steel wheels and cast iron drums at a level of 300,000 units using new equipment would cost $12.7 million where some foundry equipment was added to an existing plant, $18.7 million for plant addition together with new buildings, and $20 million for "scratch" entry with a new plant on a new site. (RX 280A) Each of these estimates [24] would be lowered by the use of used equipment (an inferior alternative for reasons explained by the witness at Tr. 4998), or production at lower levels of output.[26]

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[25] Like Judge Howder we find ourselves unable to reach any definitive conclusion with respect to overall profits in the heavy-duty wheel market. (I.D. 247) Demand for the product is somewhat cyclical, and it appears that there have been lengthy periods during which at least some of the larger and possibly more efficient industry members have enjoyed profits substantially above the norm for all industry. (*e.g.*, CX 347A-C, E *in camera*, CX 746-748 *in camera*) Moreover, the industry has experienced numerous periods of severe shortages, I.D. 253, to which the response has sometimes been expansion of capacity by existing firms, I.D. 323, (suggesting that it was profitable to do so) rather than entry by new firms, which may have been deterred by entry barriers, *see* textual discussion *infra*.

Respondent contends that Mr. Greenberg's estimates of scale economies are unreliable because they are merely "engineering" estimates and do not take account of the effect of cyclicality of demand, which *under certain circumstances* may allow a smaller plant to produce more cheaply when operating below capacity over a business cycle than a larger plant which would be more efficient if able always to operate at full capacity. As Professor Bain himself observed, however, a primary reason why this result *may* occur is that "smaller scale operations may frequently be 'less capitalistic,' in the sense of using a smaller proportion of labor and materials than larger-scale operations," thus giving the smaller plant an advantage in adjusting costs to fluctuations in production. (Bain, *supra.* p. 63) While a theoretical possibility, it has not been shown that this phenomenon operates here.[27] In our view Judge Howder [25] properly took into account the estimates of witness Greenberg in assessing scale economy barriers, and we believe his conclusion at I.D. p. 110 that these barriers are significant is supported by the preponderance of the evidence, reviewed in more detail at I.D. 224-235.

Similarly, we believe that Judge Howder properly concluded that capital barriers to entry into the heavy duty wheel market are substantial and significant. (I.D. p. 110) As Mr. Greenberg's estimates indicate, entry at an optimal level of production for spider and drums is likely to cost from $12.7 million to $20 million; entry with facilities capable of producing 200,000 units instead of 300,000 would cost from $9.1 to $15.2 million (RX 280A). The deployment of used equipment might lower these estimates somewhat, but would represent a less reliable, efficient, and therefore likely mode of entry. (Tr. 4998)

In an effort to summarize fairly the evidence of record, Judge Howder also cited evidence respecting other, sub-optimal modes of entry, including entry into ductile iron wheels (I.D. 215) and entry by substantially sub-optimal plants (I.D. 218-219). While we see no need to "strike" these findings, as complaint counsel urge, we must simply reiterate that in our view they do describe sub-optimal modes of entry, which would be likely eschewed by any firm which sought to provide significant competition to the long-established dominant firms. Accordingly we conclude that capital costs of heavy duty wheel production constitute a not insubstantial barrier to entry into that market.

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[26] Production costs might also be lower for ductile *iron* wheels as opposed to *steel* spiders, but the record indicates that iron wheels comprise a very small percentage of industry production and steel wheels are widely preferred. (I.D. 214) We thus believe that Judge Howder properly disregarded evidence regarding the cost of entry via production of cast iron spiders.

[27] Respondent's second reason for disagreeing with its witness's estimate of scale economies, *i.e.*, that wheel assembly lines may be used for more than one product (a proposition for which there is only limited record support) in some ways undermines its first, since it suggests that a 300,000 unit wheel line could be utilized for other purposes during periods of slack demand for wheels, thereby allowing realization of the full cost advantage which Mr. Greenberg's engineering estimate predicts.

The heavy duty wheel market has been characterized by recurring periodic shortages since World War II, and particularly within the past twelve years (*i.e.*, 1966, 1968-69, 1973-74; I.D. 253). The shortage in 1973-74, possibly the most severe, substantially disrupted trailer production, as various equipment manufacturers found themselves unable to locate alternative sources of supply despite their willingness to pay premium prices. (I.D. 255)

Fruehauf's role in the heavy duty wheel industry must be understood in light of its position as a major purchaser of the product, accounting for nearly 6 percent of industry purchases in the 1970-72 period. Dependent upon outside sources for its supply of heavy duty wheels, Fruehauf had strong motivation to integrate into wheels or otherwise expand their [26] supply to ensure itself a source of the product. The record reflects efforts by Fruehauf within the past decade to produce first fabricated aluminum (I.D. 282 ff.) and then fabricated steel wheels, (I.D. 294 ff.) as substitutes for those it was currently purchasing. Alternatively, Fruehauf has sought to encourage production by others as a source of supply for itself. In the late 1960's Fruehauf considered a joint venture with Webb in which Webb would guarantee Fruehauf a supply of wheels. (I.D. 280) In 1967-68, when the wheel operations of Dayton-Walther were struck, McConway and Torley decided to diversify into heavy duty wheels and sought out Fruehauf, a leading purchaser desirous of securing an additional source of supply. Fruehauf encouraged McConway and Torley in its endeavors, which are described by the ALJ at I.D. 304-305. McConway and Torley ultimately proved unable to remain profitably within the market, and it exited entirely in 1974. Fruehauf also engaged in a joint effort with U.S. Steel leading toward the production of a fabricated steel wheel, which was abandoned in September 1973. (I.D. 309-312)

It requires no feat of imagination to suppose that the foregoing pro-competitive ventures on the part of Fruehauf and those it encouraged are much less likely to be repeated now that Fruehauf has acquired a major producer of heavy duty wheels. No longer does

Fruehauf possess any incentive to encourage entry by others into heavy duty wheels. No longer does it possess any incentive to produce wheels on its own. And no longer can potential entrants into wheel production view Fruehauf as a likely source of patronage. We think that these circumstances precisely illustrate the evils of "foreclosure." In a market in which entry is no easy matter, the possible patronage of a major buyer may constitute the difference between a firm's deciding to enter and deciding not to, or between a firm's remaining within a market or leaving it. Fruehauf's ownership of Kelsey-Hayes, and the likelihood that it will turn to it for supply, means there exists one less source to which a possible entrant may look in the search for customers needed to render its entry attractive. The record suggests that a firm may require as much as 8.9 percent of the market to enter on a cost-competitive basis with the leading firms. Acquiring even part of the custom of Fruehauf can take one a long way toward that goal. [27]

While the record reflects at most a small shift of Fruehauf's patronage to Kelsey-Hayes during the pendency of this litigation (*e.g.,* I.D. 321), we agree with the ALJ that given Fruehauf's propensity to purchase in-house it is likely that at such time as this merger is no longer under a cloud Fruehauf will turn to Kelsey for supply. Certainly that is the widespread fear of competing wheel producers (I.D. 320; Tr. 2546–47) and it cannot be said to be at all unreasonable under the circumstances.[28]

A further likely anticompetitive effect of this merger may be felt in the truck trailer market, which, as observed hereinabove has suffered from periodic shortages of heavy duty wheels, at times necessitating curtailment of production. During periods of shortage one would generally expect a supplier to allocate supply among its customers, or to favor customers based upon the willingness of each to pay. With a major wheel producer now owned by a major purchaser, however, and a purchaser which has previously made strenuous efforts to find sources of supply so as to avoid the debilitating effects of shortages, we think it likely that any future shortages will find Kelsey-Hayes favoring Fruehauf, the industry's largest member, at the expense of other customers. (I.D. 319, 324) Accordingly, we believe the record warrants the conclusion that this merger may tend to substantially lessen competition by foreclosing competitors of Fruehauf from at least a portion of the supply of Kelsey-Hayes which they might require and would otherwise obtain during times of shortage. Given that output-curtailing shortages of wheels have not been an uncommon occurrence, we believe the law does not require that its likely harmful effects be shown to have occurred in fact before the merger may be condemned.[29]

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[28] Respondent argues notwithstanding Fruehauf's 5.8 percent average share of wheel purchases for 1970–72, that the actual amount of likely foreclosure should more properly be assessed as 3.9 percent of the market, representing Fruehauf's total *cast* wheel purchases. The ALJ concluded that while Kelsey-Hayes does not manufacture disc wheels for heavier truck trailers, it could readily shift production to such wheels if guaranteed an outlet for them, and he, therefore, rejected respondent's argument.

There is a certain inconsistency in respondent's position, inasmuch as it has maintained that the only relevant wheel market in this case is that for all heavy duty wheels, and that (trailer) cast wheels alone are not a separate submarket.

Nevertheless, we think that perhaps the most realistic way to characterize the situation is to say that the percentage of likely foreclosure here is a "weak" 5.8 percent or a "strong" 3.9 percent. Because of differences in disc and cast wheel production methods, Fruehauf is arguably less likely to purchase all its wheel requirements from Kelsey than otherwise. But because of similarities in both production methods and in end use of cast and disc wheels, Fruehauf is more likely to purchase in excess of 3.9 percent of all purchased wheels from Kelsey than it would be were disc and cast in fact two separate markets.

Respondent also suggests that the relevant market shares should be diluted because the ALJ failed to consider in-house production of wheel components by OEM's in tabulating the size of the market. Evidence regarding in-house production is fragmentary and suggests at most occasional machining of wheel components other than the center member by various producers to satisfy a small part of requirements. It does not appear, nor has respondent adduced any evidence to suggest that addition of such production would significantly increase the size of the market, or, thereby, significantly reduce the relevant market shares. Moreover, exclusion of in-house capacity does not in any way alter the significance of the percentages derived by the ALJ as a measure of previously unforeclosed demand for wheels which is now subject to foreclosure by virtue of the challenged merger. [28]

For the foregoing reasons, then, we conclude that respondent's acquisition of Kelsey-Hayes runs afoul of Section 7 by foreclosing Fruehauf as a source of patronage of heavy duty wheels in a market setting in which such foreclosure is likely to increase barriers to entry, make new entry more difficult and less likely, and thereby enhance the market power conferred by a highly concentrated market structure into which entry was previously difficult to begin with. Additionally we believe that the merger is likely to lessen competition substantially by foreclosing Kelsey-Hayes as a source of supply to truck trailer manufacturers should shortages of supply recur. [29]

As in the market for antiskid braking devices, our conclusion is consistent with existing precedent, albeit such precedent involves somewhat different factual situations and economic realities. The percentages of foreclosure here exceed percentages found to warrant condemnation in *Brown Shoe, supra* in a market setting involving greater concentration and equivalent or greater barriers to effective entry. The observations we have made at p. 19 *supra* with regard to ASBD apply here generally as well. [30]

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[29] As a practical matter it will always rest within the power of respondent to prevent the occurrence of anticompetitive foreclosure during the pendency of a merger challenge and accordingly the non-occurrence of such effects cannot be probative of whether they are likely to occur in the future, *Federal Trade Commission* v. *Consolidated Foods Corp.*, 380 U.S. 592, 598 (1965).

We note that even absent evidence of persistent shortages, a violation in a vertical merger may, under appropriate circumstances, be proven in the market for the end-product made by the merging customer, by virtue of foreclosure of competitors of the merging customer from access to production of the merging supplier, *e.g., Ash Grove Cement* v. *FTC*, 85 F.T.C. 1123 (1975).

POTENTIAL COMPETITION AND ENTRENCHMENT COUNTS

Like the gladiator who thrusts a second and third time towards his opponent, having first struck him directly through the heart, complaint counsel have sought to show this merger triply condemned by asserting, in addition to the traditional allegations of vertical foreclosure that the merger removed Fruehauf as a potential competitor into the heavy duty wheel market and entrenched it as the dominant firm selling truck trailers.[30] We address these contentions below.

Potential Competition

The complaint alleged as a separate theory of violation that Fruehauf, prior to its acquisition of Kelsey-Hayes, was likely to enter the heavy duty wheel market on its own, and that by virtue of its acquisition it was removed as such an entrant. Complaint counsel assert, and the ALJ concluded, that Fruehauf was one of a few, and perhaps the most significant potential entrant into the heavy duty wheel market. Fruehauf's entry, it is hypothesized, would likely have occurred at such time as wheel prices rose by a certain amount (perhaps 50 percent), but by virtue of its acquisition of a wheel supplier it is no longer likely to attempt *de novo* entry under any circumstances, thereby depriving the market of the pro-competitive influence of a significant potential entrant.

We have no quarrel with complaint counsel's legal theory, but, while a close question, we do not believe it is supported by a preponderance of the evidence. To some degree this count overlaps with the vertical foreclosure allegation. Clearly Fruehauf did exert a valuable procompetitive effect upon the heavy duty wheel market because of its status as a dissatisfied, unintegrated *customer,* eager to secure, and willing to encourage, new sources of supply by third parties as well as itself. These activities are summarized *supra* at pp. 25-26 and in the initial decision at I.D. 280-312. [31]

Viewed solely as a potential *entrant* into heavy duty wheel production, Fruehauf looms somewhat less impressive. As respondent observes (and complaint counsel do not contest) Fruehauf had no evident intention and was most unlikely to enter the market by either of the conventional means, production of cast spoke or disc wheels. Rather, Fruehauf had experimented with production of fabricated aluminum and steel wheels, but abandoned the experiments as being economically unfeasible given then-prevailing prices. (I.D. 289, 292, 299) In rejecting fabricated wheels Fruehauf was not alone; they constitute but a very tiny fraction of the wheel market, and other companies have failed in efforts to produce them economically. (I.D. 257-259) While Fruehauf retained the plans of its aborted ventures to enable it to reinstitute production in the future, it is not clear to us that it was likely to do so, barring some very large increase in prices of the sort that might well have induced other vehicle producers to consider entry themselves.[31]

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[30] A fourth thrust was intercepted at trial by Judge Howder, who dismissed the charge that the merger had entrenched Kelsey-Hayes as a dominant firm. Respondent, understandably, appears to see its adversary as more nearly like the andabata, flailing about in hopes that at least one of its blows will prove telling.

In our view then, the evidence does not demonstrate that Fruehauf was one of a few significant potential entrants into the heavy duty wheel market. Under no circumstances was it likely to attempt to breach the rather formidable barriers to entry into this market via traditional means.[32] [32] And only given very sharp price increases was Fruehauf likely to re-attempt entry via the sub-optimal means it had previously adopted. To be sure, we think it quite clear that but for its acquisition of Kelsey-Hayes, Fruehauf would have continued to agitate in procompetitive fashion for increased wheel production. But, as noted above, we think that this unfortunate effect of its merger is most properly analyzed as the consequence of its being foreclosed as a source of patronage for other wheel manufacturers and potential manufacturers, rather than exclusively as the consequence of its being removed as a potential manufacturer itself.

In dismissing the potential competition count we hasten to add that we do not find it fatal to complaint counsel's case that they have failed to prove that Fruehauf was likely to enter the market in some "near future" defined without reference to the level of prices in the market. To the extent that potential entrants, lurking on the edge of a market ready to enter serve any procompetitive function at all, it is to ensure that those already in the market do not take liberties in setting prices or other terms of sale which their market positions may allow but which are inconsistent with competitive norms. Potential entrants, when perceived as such by those already in the market, may deter anticompetitive mischief by the mere threat that they will enter should prices get out of hand. [The so-called "edge" effect. *United States* v. *Falstaff Brewing Corp.*, 410 U.S. 526, 534-35 n. 13 (1973); *United States* v. *Phillips Petroleum Co.,* 367 F. Supp. 1226, 1239 (C.D. Cal. 1973), *aff'd.* 418 U.S. 906 (1974).]

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[31] Judge Howder cites testimony by a Fruehauf employee that if the price of wheels to Fruehauf were to rise by 50 percent "it would change the whole picture" as to its entry. (I.D. 293; Tr. 5159-60)

[32] Respondent properly points to an inconsistency in complaint counsel's arguments regarding potential competition and vertical foreclosure. In seeking to measure barriers to entry, complaint counsel have done so with reference to the most desirable, efficient modes of entry. Fruehauf, of course, sought to enter in a somewhat different, less expensive way. Complaint counsel have convinced us that entry barriers into heavy duty wheels are significant; they have not convinced us that Fruehauf would likely have tried to surmount them.

Even when largely unrecognized by industry members, however, potential competitors may, as such, serve the public good by actually entering a market *at such time as* sufficiently supra-competitive price levels should make it worth their while. Should competition break out for some sustained period (as it has been known to do in even the most intensely concentrated industries) the actual potential entrant may remain just that—*potential*. But its removal via merger as an actual potential entrant may be no less a loss for competition, because such removal renders it that much more likely that once the internal impulses to competition are contained, and tacit collusion or inefficiency holds sway, there will be no firm outside the market to enter and drive prices down. [33]

From the foregoing we think it follows that the inability of enforcement authorities to demonstrate that a potential entrant is likely to enter a market in the "near future" should constitute no bar to undoing its merger with a substantial market participant, because the purpose of the law, to preserve competition and increase the likelihood that it will persist, may be satisfied whether or not the potential entrant becomes actual within some brief period of time. To require that the likely time of entry be specified in absolute terms, rather than in contingent ones, will render the law useless to preserve the beneficial effects of potential competition, because mergers by potential competitors during periods when prices approach competitive levels (and *de novo* entry is not imminently contemplated) will be immune to challenge.[33] [34]

Entrenchment

The ALJ found that Fruehauf was the dominant firm in its market and that its acquisition of Kelsey-Hayes conferred on it a significant competitive advantage, by virtue of Kelsey's manufacture of two critical components of truck trailers, ASBD and heavy duty wheels. (I.D. p. 114) Drawing on a line of cases in which "conglomerate" mergers involving dominant firms have been condemned because the mergers entrenched those firms as leaders in their market, *e.g.*, *FTC* v. *Procter & Gamble Co. (Clorox)* 386 U.S. 568 (1967), the ALJ concluded that a similar effect could be found here and assigned it as a further reason for finding a violation of law.

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[33] We do not mean to suggest that inquiry need or should necessarily be made, as it was here (Tr. 5159-60), into what prices or profit margins would induce the acquiring firm to contemplate entry. Subjective evidence such as managerial testimony that an acquiring firm would have entered *de novo* or by toehold acquisition only under highly improbable circumstances may be either too elusive or too unreliable to shed much light on the true propensity for future entry. Instead, objective evidence regarding a firm's likelihood of entering a market (*e.g.*, technological, marketing, and managerial capability, capital availability, corporate history and prior growth) may permit the inference that it would be likely to enter given a shift in market conditions. And, in turn, the likelihood of such a shift may, under appropriate circumstances, be reasonably inferred from the record. We do not believe this position need prove inconsistent with *BOC International Ltd.* v. *FTC*, 557 F. 2d 24 (2d Cir. 1977) since the Court there recognized that "near future" could be defined in terms of objective evidence such as lead time and entry barriers.

Once again this count overlaps considerably with the vertical foreclosure allegation. We agree that in one major respect its acquisition does give Fruehauf, the long-time leading firm in the concentrated truck trailer market, a significant advantage over its rivals. That, of course, pertains to the sure source of heavy duty wheels—a necessary product, often in short supply—that Fruehauf has acquired. This source of injury has previously been addressed in our discussion of the vertical foreclosure count. Whether, with respect to Fruehauf's leading position in the truck trailer market, this merger presents any further cognizable danger is a question that we need not and do not reach. [35]

REMEDY

Judge Howder, at complaint counsel's urging, recommended entry of an order requiring total divestiture of Kelsey-Hayes. Respondent has suggested on appeal that, assuming a violation is found, some form of partial divestiture, involving only assets devoted to production of ASBD and heavy-duty wheels, be imposed.[34]

The purpose of relief in Section 7 cases is to undo the probable anticompetitive effects of the unlawful merger. Restoration of competition to the state in which it existed at the time of the merger, or to the state in which it would be existing at the time relief is ordered, is the goal. Ordinarily this goal may be approached (if not altogether achieved) by restoring the acquired entity as a viable competitor in the markets in which competition has been restrained.

In pursuing this objective, we think a strong presumption favors total divestiture of the unlawfully acquired entity as the surest means of accomplishing it, *Ford Motor Company* v. *United States*, 405 U.S. 562 (1972); *United States* v. *E.I. duPont de Nemours & Co.*, 366 U.S. 316, 334 (1961); *United States* v. *Continental Can Company, Inc.*, 1964 Trade Cases, ¶71,264 at p. 80,338 (S.D.N.Y. 1964). The government will rarely be in a position to knowledgeably carve up a company into viable components. The most that can generally be asserted with any degree of confidence is that the acquired entity was a viable competi[36]tor before its acquisitions, and is thus likelier than any of its possible parts to be a viable competitor in the future. While the acquiring company may be in a better position than the government to know whether a viable partial divestiture is feasible, it is unlikely, particularly in the usual horizontal merger case, to be the most reliable arbiter, because its own self-interest favors leaving its divested competitor in a weaker, rather than stronger position.

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[34] Respondent's "Memorandum on Issues of Relief" also suggests that limitations upon purchases by Fruehauf from Kelsey-Hayes would be a satisfactory remedy. In our view, allocation of supply, while sometimes necessary, is hardly a desirable function for the government to perform. As far as we are concerned, Fruehauf should at any given time be free to buy *all* of its requirements of ASBD or heavy-duty wheels from Kelsey-Hayes if it determines, on the basis of arms-length dealing, that Kelsey is offering the best deal. Such arms-length dealing is likely to occur, however, only if ownership of the two companies is separated.

Respondent observes that this argument may have less force in the context of a vertical merger, because the respondent, rather than being required to divest a competitor which it may well wish to leave weaker, is being required to divest a customer or a supplier, which it will presumably have some interest in restoring in as strong competitive condition as possible. While there may be some theoretical validity to this observation, it nonetheless remains likely that a respondent in any merger will be desirous of retaining as large a segment of the unlawfully acquired entity as possible, and this desire will inevitably conflict with the divestiture of a viable entity if the task is left, in effect, to respondent.

In an effort to explore respondent's contention that partial divestiture in this case would be appropriate should a violation be found, the Commission ordered submission by both sides of supplemental memoranda on the issue of relief. Having reviewed these briefs we conclude that respondent has not shown that the partial divestiture it suggests would be sufficient to restore Kelsey-Hayes to its former position of strength as a seller of ASBD and heavy-duty wheels independent of Fruehauf. To the contrary, we believe that the evidence indicates that only total divestiture, or divestiture of the Kelsey-Hayes Auto Truck-Group, which comprises a major portion of the assets of Kelsey-Hayes, is likely to offer the greatest likelihood of restoring competition to its pre-merger (or "but for the merger") vigor.

Respondent suggests divestiture solely of the assets at Kelsey-Hayes' Brighton plant devoted to ASBD production, and at Kelsey-Hayes' Rockford or Gunite plant devoted to heavy duty cast spoke wheel and drum manufacture. Such partial divestiture, however, would exclude the Kelsey Products Division of the Auto-Truck Group which serves as the replacement selling and servicing arm for the Group, and is thus important in the marketing of the relevant product lines, nor would it include central corporate research and development capabilities which have played a critical [37] part in the development and refinement of ASBD. (CX 90M) In addition, while complaint counsel have perhaps somewhat overstated the extent to which certain plants in the Auto-Truck Group impinge upon the markets involved in this case, it does seem clear that some diversity of product offerings is likely to be desirable for sellers of ASBD (all but one of those currently in the market sell other braking components) and heavy-duty wheels, and certain components (such as rotors, produced at the Kelsey Kingsway plant) may be necessary in the sale of wheels (Kelsey sells wheels to a major customer in which a Kelsey spider made at Gunite is attached to a disc brake rotor made at Kingsway, Tr. 2014, 2227–2228).

Given these and other interrelationships among the segments of the unlawfully acquired corporation, we find ourselves unable to conclude that there exists a way to separate the product lines on which a finding of violation is predicated so as to preserve or restore Kelsey-Hayes, or some new entity, as a viable manufacturer and marketer [38] on a basis comparable to its pre-merger status.[35] It does appear, however, that there exists no need to require divestiture of those assets unique to Kelsey-Hayes' Aerospace [39] Group or its R-V Agriculture Group, should Fruehauf desire to retain these. Divestiture of the bulk of Kelsey-Hayes appears to be the surest way to effect the reconstitution of a viable entity independent of Fruehauf and capable of operating as a full-fledged producer of ASBD and heavy-duty wheels on the same basis as Kelsey-Hayes is now and was prior to this merger. In the event that a suitable purchaser cannot be located (or if Fruehauf prefers) the order leaves room to accomplish the required goal by means of spin-off, an alternative that would not be feasible were we to require the more limited divestiture proposed by respondent. We have, accordingly, entered an order requiring divestiture of Kelsey-Hayes except for assets unique to the Aerospace and Agriculture Groups. We have also enlarged the time in which Fruehauf must accomplish divestiture from six months to one year, in accord with general Commission practice in cases of this magnitude.[36]

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[35] The Commission's decision ordering partial divestiture in *Warner Lambert Company*, 88 F.T.C. 503 (1976) in no way compels a comparable result here. In *Warner Lambert*, having alleged violations in more than 50 submarkets, and an overall drug market, the Commission found violations in only five submarkets accounting for less than 5 percent of the acquired firm's sales. Because Parke-Davis was a minor factor in all of the submarkets in which a violation was found, and given the large number of drug companies without positions in these markets, the Commission concluded that it was very likely that the relevant Parke-Davis market positions could be transferred to other companies with no loss of viability or restraint of trade, and without the need for divestiture of corporate-wide distribution or managerial functions, 88 F.T.C. at 504–505.

In this case the markets involved account for a much greater proportion of Kelsey-Hayes' assets (see below) and Kelsey-Hayes is the leader in one market and one of the top four producers in the other. Under these circumstances we find it impossible to conclude that piece-meal divestiture of plants and production lines will suffice to preserve Kelsey-Hayes' competitive position in the hands of any acquirer which itself is not a producer or significant customer in the relevant markets.

[The parties differ on the share of sales and assets ascribable to the affected markets. Taking only Brighton and Gunite as the measure, which excludes other plants and overhead functions that may also be relevant, it appears that in 1975 Gunite accounted for $41 million of assets (CX 747M *in camera*) and Brighton for somewhere from $3 to $7 million, for a total of 17.5–19 percent of 1975 Kelsey domestic assets of $251.5 million. On a sales basis, Gunite in *1973* accounted for 7.80 percent of Kelsey's sales (CX 746A), in *1974* for 10.5 percent of sales (CX 746B, 478S *in camera*), and in 1975 for 7.5 percent of domestic sales (CX 746C, 748V *in camera*). Over a business cycle the foregoing sales percentages might be expected to rise to reflect the capital expansion which had occurred at Gunite by 1975. Brighton in 1975 accounted for 2.38 percent of Kelsey-Hayes' domestic sales. (RX 260 *in camera*)]

An appropriate order is appended.

FINAL ORDER

This matter has been heard by the Commission upon the appeal of respondents' counsel from the initial decision and upon briefs and oral argument in support thereof and opposition thereto, and the Commission, for the reasons stated in the accompanying Opinion, has denied the appeal in major part.

It is ordered, That pages 1-110 of the initial decision of the administrative law judge, and Conclusions 1-7, 9(a)-(c), 9(f) and 10 at pp. 117-119 of the initial decision, are hereby adopted as the Findings of Fact and Conclusions of Law of the Commission except as qualified and modified by the accompanying Opinion. Other Findings of Fact and Conclusions of Law of the Commission are contained in the accompanying Opinion.

It is further ordered, That the following order to cease and desist be hereby entered: [2]

ORDER

I

It is ordered, That respondent, Fruehauf, a corporation, and its officers, directors, agents, representatives, employees, subsidiaries, affiliates, successors and assigns, shall divest all stock, assets, title, properties, interest, rights, and privileges, of whatever nature, tangible and intangible, including without limitation all buildings, machinery, equipment, raw material reserves, inventory, customer lists, trade names, trademarks and other property of whatever description, excluding the operations unique to Kelsey-Hayes'

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[36] While the record permits no conclusion other than that divestiture of the bulk of Kelsey-Hayes is necessary to undo the effects of the unlawful acquisition, we do observe that Section 3.72 of the Commission's Rules of Practice permits a party under order to seek reopening of the order if it can demonstrate that changed circumstances so warrant. If Fruehauf, contrary to what now appears likely from the record, is able to secure a purchaser of the Gunite and Brighton plants, which is not itself a manufacturer or purchaser of ASBD or heavy-duty wheels, and which appears likely to be able to operate these plants so as to maintain the leading position in the sale of ASBD and heavy-duty wheels now held by Kelsey-Hayes, the Commission will consider reopening of its order.

The filing of such a petition to reopen will, under no circumstances, constitute grounds for delay of Fruehauf's obligation under the order we have entered to divest the bulk of Kelsey-Hayes. Given that the record indicates that sale or spin-off of the bulk of Kelsey-Hayes is the only approach that is likely to remedy the violation of law, the Commission believes that the law would be disserved by permitting delay in implementation of the indicated remedy while respondent made what presently appear likely to be vain attempts to effect a different remedy. However, the Commission does not wish to preclude Fruehauf from making a clear and convincing showing (via production of a suitable purchaser) that the remedy it has proposed would suffice, provided Fruehauf desires and is able to attempt such a showing without imposing delay in effectuation of the remedy that the record before us indicates is warranted.

Aerospace Group and its R-V Agriculture Group, acquired by Fruehauf as a result of its acquisition of Kelsey-Hayes together with all additions and improvements to Kelsey-Hayes which have been added to Kelsey-Hayes subsequent to the acquisition (excluding those improvements unique to the Aerospace Group and the R-V Agriculture Group). Such divestiture shall be absolute, shall be accomplished no later than one year from the effective date of this order, and shall be subject to the prior approval of the Federal Trade Commission.

II

It is further ordered, That such divestiture shall be accomplished absolutely to an acquirer approved in advance by the Federal Trade Commission so as to transfer Kelsey-Hayes as a going business and a viable, competitive, independent concern.

III

It is further ordered, That pending any divestiture required by this order, Fruehauf shall not knowingly cause or permit the deterioration of the assets and properties specified in Paragraph I in any manner that impairs the marketability of any such assets and properties. Fruehauf may, but shall not be required to make capital expenditures for the improvement of any such assets and properties.

IV

It is further ordered, That pursuant to the requirements of Paragraph I, none of the stock, assets, properties, rights, privileges and interests of whatever nature, tangible or [3] intangible, acquired or added by Fruehauf, shall be divested, directly or indirectly, to anyone who is at the time of the divestiture an officer, director, employee or agent of, or under the control, direction or influence of Fruehauf, or anyone who owns or controls, directly or indirectly, more than one (1) percent of the outstanding shares of the capital stock of Fruehauf or to anyone who is not approved in advance by the Federal Trade Commission.

V

It is further ordered, That for a period of ten (10) years from the date this order becomes final, Fruehauf shall cease and desist from acquiring, or acquiring and holding, directly or indirectly, through subsidiaries or otherwise, without the prior approval of the Federal Trade Commission, the whole or any part of the stock, share capital, assets, any interest in or any interest of, any concern, corporate or noncorporate, engaged in the business of manufacturing, distributing, or selling, heavy duty wheels, heavy duty antiskid braking devices, or truck trailers, nor shall Fruehauf enter into any agreement, understanding or arrangement with any such concern by which Fruehauf obtains the market share, in whole or in part, of such concern in the above-described product lines.

VI

It is further ordered, That on the first anniversary date of the effective date of this order and on each anniversary date thereafter until the expiration of the prohibitions in Paragraph V of the order, Fruehauf shall submit a report in writing to the Federal Trade Commission listing all acquisitions, mergers and agreements to acquire or merge made by Fruehauf; the date of each such acquisition, merger or agreement; the products involved and such additional information as may from time to time be required.

VII

It is further ordered, That within thirty (30) days from the effective date of this order and every sixty (60) days thereafter until it has fully complied with Paragraph I of this order, Fruehauf shall submit a verified report in writing to the Federal Trade Commission setting forth in detail the manner and form in which it intends to comply, is complying or has complied therewith. All such reports [4] shall include, in addition to such other information and documentation as may hereafter be requested, (a) a specification of the steps taken by Fruehauf to make public its desire to divest Kelsey-Hayes, (b) a list of all persons or organizations to whom notice of divestiture has been given, (c) a summary of all discussions and negotiations together with the identity and address of all interested persons or organizations, and (d) copies of all reports, internal memoranda, offers, counter-offers, communications and correspondence concerning said divestiture.

VIII

It is further ordered, That Fruehauf shall notify the Commission at least thirty (30) days prior to any proposed changes which may affect compliance obligations arising out of the order, such as dissolution, assignment, or sale resulting in the emergence of successor corporations, and that this order shall be binding on any such successor.

IN THE MATTER OF

REICHHOLD CHEMICALS, INC.

ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT AND SECTION 7 OF THE CLAYTON ACT

Docket 9076. Complaint, March 11, 1976 — Final Order, Feb. 22, 1978

This order, among other things, requires a White Plains, N.Y. manufacturer and distributor of various products, including fiberglass reinforced panels (frp panels) to divest itself completely, within one year from service of this order, of The Corrulux Corporation, a Houston, Tex. producer of frp panels. Further, the firm is prohibited, for a two-year period, from soliciting (for the purpose of selling fiberglass reinforced plastic panels) those customers who had purchased such panels from Corrulux during the year prior to its acquisition by RCI. Additionally, the order prohibits RCI from acquiring, for ten years, any domestic company engaged in the production, sale or distribution of frp panels.

Appearances

For the Commission: *Charles W. Corddry, III, Steven A. Newborn* and *Max C. Dorian.*

For the respondent: *John Boyer* and *Adrian C. May, Jr., Cadwalader, Wickersham & Taft,* New York City and Washington, D.C.

COMPLAINT

The Federal Trade Commission having reason to believe that Reichhold Chemicals, Inc., a corporation subject to the jurisdiction of the Commission, has acquired Corrulux Corporation, a corporation subject to the jurisdiction of the Commission in violation of Section 7 of the Clayton Act, as amended, (15 U.S.C. 18) and Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45), and that a proceeding in respect thereof would be in the public interest hereby issues this complaint, stating its charges as follows:

I. *Respondent*

1. Respondent, Reichhold Chemicals, Inc. (hereinafter "RCI") is now and was at the time of the acquisition a publicly held corporation chartered and operating under the laws of the State of Delaware, with a principal place of business at the RCI Building, 525 North Broadway, White Plains, New York.

2. RCI is a leading manufacturer and marketer of a wide range of

synthetic resins and industrial chemicals as well as the nation's largest producer of fiberglass-reinforced plastic panels.

3. In 1973, RCI had revenues in excess of $294 million and net income in excess of $11 million. In that year RCI was the 448th ranked industrial corporation in the Fortune 500.

4. In 1974, RCI had revenues in excess of $480 million, assets in excess of $229 million and net income in excess of $24 million. In that year RCI was the 347th ranked industrial corporation in the Fortune 500. [2]

5. At all times relevant herein, RCI sold and shipped its products in interstate commerce throughout the United States and was and is now engaged in commerce as "commerce" is defined in the Clayton and Federal Trade Commission Acts.

II. *Corrulux Corporation*

6. Prior to the acquisition hereinafter set forth, Corrulux Corporation (hereinafter "Corrulux") was a corporation chartered and doing business under the laws of the State of Texas with a principal place of business located at 410 Holmes Road, Houston, Texas.

7. In 1973, Corrulux had revenues of approximately $3 million and assets in excess of $1.2 million.

8. Corrulux was, prior to the acquisition, hereinafter set forth, an independent and profitable company. In 1973 substantially all of Corrulux's sales were of fiberglass-reinforced plastic panels.

9. At all times relevant herein, Corrulux sold and shipped its products in interstate commerce throughout the United States, and was and is now engaged in commerce as "commerce" is defined in the Clayton and Federal Trade Commission Acts.

III. *The Acquisition*

10. On or about August 19, 1974, pursuant to an agreement between RCI and Corrulux, respondent purchased the assets of Corrulux for approximately $675,000 and assumed debts of approximately $1 million.

IV. *Trade and Commerce*

11. The relevant geographic market is the United States as a whole.

12. The relevant product market is the manufacture, and sale of fiberglass-reinforced plastic panels (hereinafter "frp panels").

13. Frp panels are light weight, predominantly translucent,

shatter-resistant building products composed primarily of polyester resins reinforced with fiberglass matting. [3]

14. In 1973, the year prior to the acquisition, total sales of frp panels at the manufacturing level were approximately $60 million in the United States. In 1974, the year of the acquisition, total sales of frp panels at the manufacturing level were approximately $75 million in the United States.

15. Frp panels have many different uses, some of which are, residential patios and awnings, greenhouses and the skylights of prefabricated metal buildings.

16. Before the acquisition of Corrulux there were nine major producers of frp panels accounting for over 95 percent of all frp panels sold nationally. Concentration was extremely high in 1973 with the top four and eight ranking firms accounting for over 72 percent and over 94 percent respectively. After the acquisition the top four and eight ranking firms accounted for over 77 percent and 98 percent respectively.

17. In 1973, RCI was the second ranked domestic producer of frp panels with sales in excess of $11 million. In that year RCI accounted for approximately 18.9 percent of total domestic sales of frp panels.

18. In 1973 Corrulux was the seventh ranked domestic producer of frp panels with sales of approximately $3 million. In that year Corrulux accounted for approximately 5.0 percent of total domestic sales of frp panels.

19. As a result of the aforesaid acquisition, RCI became the first ranking firm in the frp market, accounting for approximately 24.0 percent of total domestic sales of frp panels.

20. As a result of the aforesaid acquisition, concentration among the top four and eight firms increased from approximately 72 percent and 94 percent to approximately 77 percent and 98 percent respectively.

21. Prior to the aforesaid acquisition RCI and Corrulux were substantial and actual competitors in the manufacture and sale of frp panels.

V. *Effects of the Acquisition*

22. The effect of the aforesaid acquisition may be substantially to lessen competition or to tend to create a monopoly in the manufacture and sale of frp panels throughout the United States in the following ways, among others: [4]

(a) Substantial actual competition between RCI and Corrulux has been eliminated;

(b) The ability of RCI's competitors to compete in the manufacture, sale and distribution of frp panels has been, and/or may be, further substantially diminished;

(c) Concentration has been and/or may be increased to the detriment of actual as well as potential competition;

(d) RCI has become the dominant producer of frp panels.

VI. *The Violation Charged*

23. The acquisition by RCI of Corrulux constitutes a violation of Section 7 of the Clayton Act, as amended, (15 U.S.C. 18).

24. The acquisition by RCI of Corrulux constitutes an unfair method of competition in commerce and an unfair act or practice in commerce in violation of Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45).

INITIAL DECISION BY MORTON NEEDELMAN, ADMINISTRATIVE LAW JUDGE

JULY 19, 1977

I

STATEMENT OF THE CASE

The complaint in this proceeding issued on March 11, 1976. It charges that respondent, Reichhold Chemicals, Inc., has violated Section 7 of the Clayton Act (15 U.S.C. 18) and Section 5 of the Federal Trade Commission Act (15 U.S.C. 45) by acquiring the assets of The Corrulux Corporation on August 19, 1974. According to the complaint, the effects of the [2] acquisition may be substantially to lessen competition or tend to create monopoly in the manufacture and sale of fiberglass-reinforced plastic panels (hereinafter frp panels) throughout the United States.

Respondent filed an answer on April 27, 1976, in which it admitted making the challenged acquisition. It also admitted certain corporate and jurisdictional facts, but Reichhold denied the substantive allegations of the complaint relating to the existence of an frp panel relevant product market and the charges respecting the alleged anticompetitive effects of the acquisition in this market. In addition, respondent said in its answer —

> . . .that on or about October 1, 1975, the manufacturing facilities of Corrulux were shut down as a result of the fact that Corrulux's physical production facilities could not be preserved as a viable production unit without virtual replacement of such facilities. Respondent avers that at all times relevant to this proceeding, Corrulux was and is a failing company. (Answer, ¶ 25.)

In the prehearing stage both sides were allowed limited discovery, complaint counsel's requests for admissions were answered, and stipulations were filed. Upon completion of the prehearing stages, the case-in-chief began on January 17, 1977 and ended on January 28, 1977. The defense case was presented between February 28, 1977 and March 9, 1977. A hearing for rebuttal was held on April 20, 1977.[1] During the hearings all counsel were given full opportunity to be heard, and to examine and cross-examine witnesses. [3]

The record was closed on April 20, 1977. Proposed findings of fact and briefs were filed by the parties on May 20, 1977. Answering briefs were filed on June 6, 1977.

After reviewing all the evidence as well as the proposed findings and briefs submitted by the parties, and based on the entire record, I make the following findings of facts:[2]

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[1] This unusually long interval between hearings was allowed to encourage the parties to explore the possibility of a settlement. (See Tr. 2235.)

[2] Proposed findings not adopted in the form proposed or in substance are rejected, as either not supported by the entire record or as involving immaterial or irrelevant matters.

The following abbreviations are used throughout in citing to the record: "Tr." (transcript of testimony); "CX" (complaint counsel's exhibit); "RX" (respondent's exhibit); CX 1, an index to complaint counsel's exhibits, contains a description of each document and the date received in evidence or rejected. The same information for respondent's exhibits appears on RX 1. CX 1 and RX 1 also indicate which exhibits are *in camera*. By the terms of my *in camera* rulings there is no limitation whatever on the public use of this material in decisions written by the undersigned, the Commission, or other reviewing authorities. (Tr. 294-96.) As I indicated on the record (Tr. 295-96) it is my intention that *in camera* status will end on January 1, 1979 when *in camera* exhibits are to be placed on the public record except for CX's 308A-C, *in camera*, which are to remain *in camera* without time limitation. (Tr. 298.)

The appearances of the witnesses were as follows: [4]

NAME	*CALLED BY*	*TR. PAGES*
Joseph S. McDermott Reinforced-Plastic Composites Institute, a Division of the Society of the Plastics Industry, Inc. (Trade Association)	Complaint Counsel ("c.c.")	223-274
Victor Alfred Maynard Filon Division of Vistron, a subsidiary of the Standard Oil Company of Ohio (Frp Panels Manufacturer)	c.c.	304-446
David A. Yundt Resolite Division of H.H. Robertson Company (Frp Panels Manufacturer)	c.c.	452-529
Jay Paul Feder Barclay Industries, Inc. (Frp Panels Manufacturer)	c.c.	533-620
Michael Cafarchia Lasco Division of Phillips Industries, Inc. (Frp Panels Manufacturer)	c.c.	625-692
Robert E. Simpson (Former owner of Corrulux)	c.c.	702-828
Alfred B. Menzer Kemlite Corporation (Frp Panels Manufacturer)	c.c.	832-915

(Continued)

[9] II

FINDINGS OF FACTS

REICHHOLD AND CORRULUX

1. Respondent, Reichhold Chemicals, Inc. (hereinafter Reichhold) is a Delaware corporation with its principal place of business located at 525 North Broadway, White Plains, New York. (Complaint and Aswer ¶ 1.)

2. Reichhold is a major manufacturer and marketer of a wide range of synthetic resins and industrial chemicals, as well as frp panels. (CX's 6F, J, K.)

3. In 1973, the year prior to the subject acquisition, Reichhold's total sales were $294 million. (Complaint and Answer ¶ 3.)

4. In 1973, Reichhold's sales of frp panels were about $12 million. These panels were produced by Reichhold's Reinforced Plastics Division at plants located in San Diego, California and Grand Junction, Tennessee. (Admissions 2, 3, CX's 305B, M, CX's 13C–E; Tr. 1891.) Frp panels are the only end-use or consumer products produced by Reichhold — basically, respondent is a manufacturer of raw materials such as the resins and chemicals used by the plastics industries. (CX's 5A–10Z–19.)

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[5] Jerry G. Christopher Glasteel, Inc. (Frp Panels Manufacturer)	c.c.	920–1045
Davis Allen Marathon Metallic Building Co., a subsidiary of Marathon Manufacturing Company (Pre-engineered Metal Building Manufacturer)	c.c.	1051–1091
Roger D. Hertel IBG-Roper Industries, Inc. (Greenhouse Manufacturer)	c.c.	1093–1129
Frederick E. Reiling Fiber Glass Plastics, Inc. (Frp Panels Manufacturer)	resp.	1140–1169
David Clair Bush Idaho Chemicals Industries, Inc. (Frp Panels Manufacturer)	resp.	1170–1232
Waldo Everett Stransky Thorolyte Fiberglas, Inc. (Frp Panels Manufacturer)	resp.	1233–1279
Robert S. Morrison Molded Fiberglass Companies (Frp Panels Manufacturer)	resp.	1284–1375
[6] James Veenema Lunn Laminates, Inc. (Manufacturer of "sandwich" panels)	resp.	1376–1423

(Continued)

5. Prior to the acquisition, The Corrulux Corporation (hereinafter Corrulux) was a Texas corporation with its principal place of business and manufacturing facility located at 410 Holmes Road, Houston, Texas. (Complaint and Answer ¶ 6.)

6. In fiscal 1973 (year ending June 30, 1974) Corrulux had sales of approximately $3 million. Virtually all of Corrulux's business was derived from the sale of frp panels. (Complaint and Answer ¶ 8; CX's 3D, 307C, *in camera;* Tr. 710.) [10]

7. Prior to the Reichhold acquisition, all the stock of Corrulux

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James Allemand M.C. Gill Corp. (Specialty Panels Manufacturer)	resp.	1434-1471
Robert P. McCarthy Butler Manufacturing Company (Pre-engineered Metal Building Manufacturer)	resp.	1483-1521
Charles Pope Wrisco Inc. (Distributor to Custom Awning Fabricators)	resp.	1522-1561
Edward J. Liczwek Sears, Roebuck & Co. (Chain retailer)	resp.	1580-1616
Donald M. Reynolds Aetna Plastics Co. (Distributor of plastics)	resp.	1620-1662
Vincent Pisano Reichhold Chemicals, Inc. (Comptroller)	resp.	1663-1693
Gerhard L. Schultz IBG-Roper Industries, Inc. (Manufacturer of Greenhouses)	resp.	1699-1789
[7] John F. Doherty *Industrial Equipment News* (Trade Publication)	resp.	1798-1816
Edward E. Shea Reichhold Chemicals, Inc. (Chairman of the Board)	resp.	1822-1887
Charles Frizzelle Reichhold Chemicals, Inc. (General Manager, Reinforced Plastics Division)	resp.	1888-2002
John Marshall Mitchell Cincinnati Milacron Inc. (Frp Panels Manufacturer)	resp.	2008-2029
Thomas P. Shumaker Reichhold Chemicals, Inc. (Executive Vice President)	resp.	2029-2088
Sidney Graham Winter, Jr. Yale University (Economist — expert witness)	resp.	2089-2221
James I. Sturgeon Federal Trade Commission (Economist — expert witness)	c.c.	2250-2358

[8] In addition to this formal testimony, the record contains two depositions identified as follows:

RX 83 (62 pages) Deposition of Richard R. Keller Kalwall Corporation (Frp Panels and Sandwich Panels Manufacturer)

RX 89 (21 pages) Deposition of Maurice Horn Ornyte Division of Berdon, Inc. (Frp Panels Manufacturer) was owned by one Robert E. Simpson. (Admission 17, CX's 305C, M; Tr. 703.)

8. On August 19, 1974, Reichhold purchased the assets of Corrulux from Simpson for $675,000 and assumed Corrulux's liabilities of approximately $1 million. (Complaint and Answer ¶ 10.) The assets purchased by Reichhold included cash, receivables, inventories, machinery and equipment, trucks and autos, deposits, leases, option rights, contracts and agreements, the corporation name, patents, trademarks and technology, and all other assets including intangibles. (CX 14A.)

"COMMERCE"

9. At all times relevant to this case Reichhold and Corrulux were engaged in commerce in the manufacture, sale, and distribution of frp panels as "commerce" is defined in the Clayton and Federal Trade Commission Acts. (Complaint and Answer ¶ 5; Admission 26, CX's 305D, N.)

THE GEOGRAPHIC MARKET ("SECTION OF THE COUNTRY")

10. The parties have stipulated that the relevant geographic market ("section of the country") for evaluating the Reichhold acquisition of Corrulux is the entire United States. (Admission 74, CX's 305J, O.)[3] [11]

THE PRODUCT MARKET ("LINE OF COMMERCE")

11. Frp panels are building materials made mainly of polyester resin[4] reinforced with fiberglass. (Complaint and Answer ¶ 13.)[5] According to the complaint, the manufacture of frp panels is the only relevant product market for evaluating the effects of Reichhold's acquisition of Corrulux. Definition of the relevant product market is the threshold issue in this horizontal acquisition case, and the issue which most sharply divided the parties throughout this proceeding.

12. It is complaint counsel's position that frp panels constitute a

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[3] Frp panels are light and can be packaged in compact bundles for shipment at relatively low freight cost throughout the United States. They are also relatively easy to handle in a warehouse. While the frp panel producer located closest to a particular customer has a freight advantage, there is no evidence that this advantage is decisive. (See CX 3F.)

[4] Polyester resin is a thermosetting plastic which converts from liquid to solid by the chemical reaction of heat and catalysts. Once the resin has been cured, it cannot be reformed into a liquid state. In contrast, the more expensive thermoplastic resins such as acrylics, polycarbonates, polyethylene, polystyrene, polypropylene and butyrates can be reformed by the application of heat and pressure. (Tr. 327-29.)

[5] Other raw materials used in frp panel manufacture are styrene monomer, acrylic monomer, peroxides, filler materials, cellophane, pigments, methyl methacrylate monomer, and Tedlar. The fiberglass reinforcing material constitutes 22 to 25 percent of the panel; most of the balance is made up of polyester resin. (Tr. 309, 424, 477-78, 640-41, 835-36, 1171.)

relevant market because the product meets some but by no means all of the criteria of *Brown Shoe*[6] in which the Supreme Court said that within broader general markets, relevant submarkets may exist for Section 7 analysis by reason of industry or public recognition, peculiar characteristics and end [12] uses, unique production facilities, distinct prices, sensitivity to price changes, and the existence of specialized vendors.

13. Respondent, on the other hand, contends that frp panels are only one of many building materials that compete against each other for use in certain applications. As respondent would have it, the production of frp has no independent economic significance and the relevant market for evaluating this acquisition should at least include aluminum panels, glass, polyethylene film, and other plastic glazing materials which can be used in the same applications as frp panels.

Physical Characteristics

14. The physical characteristics of frp panels are not in dispute. Frp panels combine lightness of weight with a high degree of tensile strength and durability. The product is rigid, shatter-resistant, unaffected by moisture or moderately high temperatures, and withstands the corrosive effects of caustics, acids, and solvents.

Frp panels can be formed into configurations which "nest" with other building materials and frp panels can be made with varying degrees of translucence (up to 95 percent light transmission) thus permitting the passage of diffused light. Frp panels cannot be made transparent because of the light deflecting quality of the fiberglass ingredient. Completely opaque frp panels are used in certain applications. (Complaint and Answer ¶ 13; CX's 122F, 190-o; Tr. 227, 329, 332-34, 455-56, 559-60, 643, 833, 944-45, 1171-72.)

15. No other single product has the same combination of physical characteristics as frp panels. (Tr. 329, 550, 944.)

16. Frp panels are produced in various weights and sizes ranging from less than three ounces per square foot to 16 ounces per square foot. The most common [13] sizes are approximately 26 to 50 inches in width, six to 16 feet in length. The surface finish of the panels can be either smooth or textured. The configuration of frp panels can be flat, corrugated, or ribbed and the panels can be produced in many different colors. (CX 190-o; Tr. 330-35, 558-60, 641-42, 833-34.)

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[6] *Brown Shoe Co. v. United States*, 370 U.S. 294 (1962).

Production Facilities

17. Frp panels have been produced by three processes: the hand lay-up, the molded press, and the continuous line methods. (Findings 18–20.)

18. Production of frp panels originated in the early 1950's with the use of the hand lay-up method in which panels were made one at a time. In this process a cellophane sheet is placed in a frame shaped to the desired configuration. A fiberglass mat (fiberglass in gauze-like form) is then placed on top of the cellophane sheet and polyester resin is poured over and through the mat. A second cellophane sheet is laid on top of the resin and fiberglass. The panel is cured in an oven and cut to the desired size. (Tr. 479–82, 524–25, 571, 848–49, 926, 1176–77, 1237–38, 1700.) Although the hand lay-up method is no longer suitable for production of large volume runs, it is still the best and sometimes the only practical method for making panels of special weights, colors, and other properties, and for limited production runs. (CX 3G; Tr. 482–85.) The hand lay-up method entails significantly higher labor and raw material costs than the continuous line process and does not produce panels of uniform thickness. (Tr. 480–81, 846–47.)

19. The press molding method is similar to the hand lay-up method; in place of the frame, however, the manufacturer uses an hydraulic press containing a matched set of metal dies mounted on the faces of the press. A fiberglass mat is placed on the lower of the two faces and polyester resin mixed with pigment and fillers is spread over the mat. The press, which is heated [14] either by electricity or by steam, is closed to start the curing process. A cured panel is made in two minutes. The dimensions of the panel are determined by the dimensions of the dies. (CX 122H; Tr. 839–40, 2016–17.) The press molding method is used exclusively by two firms, Cincinnati Milacron and Molded Fiberglass, which manufacture panels for the liner application. (Tr. 1290–91, 2010, 2016; see Findings 45–54.) In addition, both Reichhold and another producer, Kemlite, use press molding for limited production runs and for specialty items.[7] (Tr. 838–39, 851, 926–27, 1977–78.) The molded press method produces perhaps the best panels because this method allows for strict control over thickness and color distribution. (Tr. 927–28.)

20. The continuous line process, which now predominates throughout the industry, is the only competitively feasible way to produce panels in large volume. In addition to speed of production,

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[7] Kemlite, for example, uses a press mold to make a high-priced ribbed liner panel which cannot be made on a continuous line. Sales of this product are being phased out. (RX's 15A–B; Tr. 852–53.)

the continuous line process reduces labor and raw material costs and produces products of uniform dimensions and quality. The process, which was originated by Filon in 1952, involves the production of frp panels on machinery which in effect produces one continuous sheet so long as raw materials are fed into the machine.[8] The continuous line machine, which typically varies in length between 250 to 385 feet, uses cellophane as a moving carrier [15] belt. Polyester resin and fiberglass rovings[9] (chopped fiberglass fibers) are dropped onto the moving cellophane belt. Pigments and fillers are added as required by a particular order. A second layer of cellophane is pressed upon the mixture of resin and fiberglass, and the carrier moves through a series of ovens which accelerate the chemical curing process. Finally, the carrier reaches forming "shoes" or dies which create the desired configuration such as the widely used sine-shaped corrugation.[10] After passing over the forming shoes, the layers of cellophane are removed and the hardened panels are trimmed and then sheared or sawed to standard lengths or to a custom length specified by the user. Continuous line machines are used solely for the production of frp panels. (CX 3H; Tr. 231, 310-14, 377-78, 479, 484, 490, 535-39, 628-32, 835-36, 849, 924-29, 1158, 1179.)

21. Except for the limited number of instances noted earlier (see Findings 19, 20), all of the producers of frp panels essentially use the continuous line process. (CX's 306A, B; RX 83, pp. 9-10; Tr. 311, 313-14, 928, 1180.)

End Uses

22. Most frp panels are sold for use in the residential, industrial, and greenhouse applications. [16]

TABLE 1: 1974 SHIPMENTS OF FRP PANELS BY USE

	% of Total Square Feet Shipped
Residential	46.5%
Industrial	36.1%
Greenhouses	10.8%
Farm	4.0%
Others	2.9%

(Source: CX 316)[11]

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[8] A modern continuous line machine can produce frp panels at linear speeds as high as 75 feet per minute for light panels but speeds of 20 to 50 feet per minute are more common. Heavier industrial panels (usually weighing eight to 12 ounces) are produced at lower line speeds of 12 to 18 feet per minute. (RX 89, p. 6; Tr. 313, 409, 539, 629, 662, 836-37, 925-26, 990, 1158-59.)

[9] One producer has an inefficient continuous line machine which requires the use of more expensive fiberglass mat instead of rovings. (Tr. 1258.)

[10] By changing the forming "shoes," a wide variety of configurations can be produced. (Tr. 332, 642, 943, 2071.)

[11] In terms of dollar volume, the heavier and more expensive industrial panels may account for a larger share of sales. (Compare Tr. 957 with Tr. 1040.)

23. No other building material identified in the record has the same range of applications as frp panels. (Tr. 329; see RX 14.)

The Residential or Patio Application

24. Conspicuous on the suburban landscape of the United States is that part of the single-family home known as the "patio."[12] This backyard area may or may not have an awning-like covering. If the homeowner opts for such a cover, there is a good likelihood that a choice will be made between a covering made of either aluminum panels or frp panels. (Tr. 1909-10, 1585-86.)

25. The so-called residential or patio application, which includes such other residential uses as fences around swimming pools, carports and carport covers, windbreakers, room dividers, decorator screens, and the [17] "skirts" of mobile homes (when they are not mobile),[13] accounted for approximately $20 million in sales at the manufacturing level in 1974. (CX's 69B, 71F, 76A, 93D, 95C, 96A, 216A-232T; Tr. 335, 945, 1581.)[14]

26. Patio covers are the most important single "residential" application for frp panels. (Tr. 1619.)

27. The basic frp panel product used in the residential or patio application is the four ounce, 2 1/2 inch sine-wave corrugated panel,[15] which is six to 12 feet long and 26 inches wide. (Tr. 435-36, 557, 956-57.)[16]

28. The functional advantage of diffused light transmission — *i.e.,* translucency — is the primary reason for the purchase of frp panels for the patio application. (Tr. 336, 583, 644, 946-47, 1590.)[17] [18]

29. Manufacturers of frp panels stress the translucence of their products in promoting them for the patio application.[18]

30. Aluminum panels, in contrast to frp panels, provide the

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[12] See Tr. 337.

[13] See CX 24B.

[14] Manufacturers who reported their sales to the Fiberglass Reinforced Panel Council in 1974 sold 101.5 million square feet of frp panels for residential use. (CX 57-o.) Typically, these panels were sold at 19¢ per square foot by frp manufacturers (Tr. 437, 1966) which would mean residential use frp sales in excess of $19 million. Ornyte did not report its sales to the Council. If Ornyte's sales are included, the dollar volume of residential sales may be as high as $24 million. (See RX 89, p. 7, 11.)

[15] See CX 194E.

[16] Some lighter panels and some five ounce panels are sold for residential use. (Tr. 686, 957.)

[17] There are some frp panels used in the patio application which are designed to reduce translucency. (CX 69A; Tr. 663.)

[18] This includes the promotions of Reichhold ("The panels block out the sun's harsh ultra-violet rays. Only soft, glare-free light passes through Alsynite/Structoglas," CX 26B; see also CX's 24A, 76A, B); Glasteel ("Wherever you want to keep the glare out - let the light in - Glasteel Fiberglass Panels," CX 95B; see also CX's 93D, 99A, 100A,

(Continued)

functional advantage of shade in the patio application. (Tr. 552, 583-84, 1541, 1590-91.)

31. In the patio application, frp panels and aluminum panels are sold to homeowners in the following ways:

(a) Custom awning fabricators use aluminum panels overwhelmingly in their installation of patio covers.[19] Only relatively small amounts of frp panel patios are installed by custom fabricators. Thus, Wrisco, identified in the record as the only national distributor of frp panels to the custom awning trade (Tr. 1533-34), [19] had 1974 sales of frp panels of $663,000 while its sales of aluminum panels were $2,775,000. (Tr. 1535.)[20]

(b) Sears, Roebuck sells complete patio kits which include both the support and the cover. The covers for these kits are made of aluminum only. (Tr. 1605.) These kits may be purchased through the Sears catalog and are installed by the homeowner on a do-it-yourself basis, or Sears will arrange for professional installation. (Tr. 1604-05.)

(c) The "do-it-yourself" homeowner, who is in the market for panels *only*, leans heavily towards frp panels. (Tr. 1596-97.) In general the bulk of the sales of frp panels for the patio application are in the form of sales of panels only through mass merchandisers like Sears. (Tr. 1546, 1596-97, 1603-05.) In contrast, aluminum panels are usually sold in the form of complete patio kits or are installed by custom awning fabricators. (See Finding 31(a), (b).) [20]

The record does not contain a satisfactory explanation for either the frp or the aluminum patterns of distribution and consumption except for evidence that custom awning fabricators clearly favor aluminum as an awning material. (Tr. 1543.) The shading and color qualities of aluminum were cited as factors behind this preference, but it is also apparent that there are higher margins to be had on the custom installation of aluminum. (See note 22, *infra* and Tr. 1543, 1554-55.)[21]

32. In setting their prices, producers of frp panels do not take into account the prices for aluminum panels nor are their prices for frp panels sensitive to the demand or to the prices for aluminum panels. (Tr. 336, 413-14, 582-83, 615-16, 636-40, 934-39, 1208, 1231-32.)

33. At the homeowner level, the prices of frp panels and aluminum panels in the patio application tend to be different. As indicated earlier, with the exception of custom installation (see

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101, 102, 103); Filon ("Filon translucent panels give you shelter - yet let you keep your sky" CX 217B; see also CX's 216A, B, 217A, 220A, B, 226A, B, 227A, B, 228A-E, 229A-E, 232A-T); and Barclay ("Barclite is able to take full advantage of the free daylight yet remove the harmful, glaring qualities of raw sunlight," CX 229B).

[19] Custom awning fabricators are part of the home improvement industry. They buy component parts including panels from a distributor and construct patios and carports for homeowners on a custom basis. (Tr. 1523-24.)

[20] In the custom installation of frp panels the more expensive six and eight ounce panels are used in contrast to the four ounce frp panels bought by the do-it-yourself homeowner. (Tr. 1526.) The use of six ounce frp panels in the custom trade tends to produce sharp differences in the prices paid by custom awning fabricators for frp and aluminum. Six ounce frp panels are sold to custom fabricators at 61¢ per square foot as compared to 43¢ for aluminum. (Tr. 1528, 1532.) Differences and fluctuations in the prices of the two materials, however, have had little effect on sales to custom fabricators: sales of aluminum to the custom trade are consistently going up, while frp panel sales to installers have been on the decline. (Tr. 1549-51.)

[21] There is no substantial evidence that this pattern is based on ease of installation. While frp panels are easy to work with, and do not require either special skills or special tools for installation — a selling point which frp panel producers have emphasized (CX's 24B, 26B, 69A, 76A, 93C, D, 96B; Tr. 227, 550, 946, 1987) and which might explain why do-it-yourselfers choose frp panels rather than kits or professional installation — the record indicates that aluminum panels, too, are relatively easy to install. (Tr. 1617-18.)

Findings 27, 31, note 20 and Tr. 1586, 1610-11), the principal frp product used in the patio application is the four ounce, sine-wave corrugated panel. This panel was sold by Sears for 35¢ per square foot in 1976. (CX 309-Z-76; Tr. 1586, 1610-11.) At the same time, mill-finished four ounce aluminum panels, metallic color, were sold [21] through the Sears catalog for 44¢ per square foot, and white-finished aluminum panels were sold by Sears for 56¢ per square foot. (CX 309-Z-76; Tr. 1587.)[22] Heavier (five ounce) frp panels are sold by Sears at approximately the same price as aluminum panels. (CX 309-Z-76; Tr. 1586-88.)

34. The overall pattern in the patio application is that most homeowners choose aluminum either in the form of custom installed aluminum patios or aluminum patio kits. (Tr. 946, 1589-90, 1598-99, 1603-05.) Frp panels are favored by "do-it-yourself" homeowners who economize by neither buying kits nor using custom installers, and prefer the muted light transmitting quality of frp panels over the shading quality of aluminum. (Tr. 336, 583, 946, 1541-42, 1590, 1598.)

THE INDUSTRIAL APPLICATION

Skylights and Sidelights

35. One of the principal industrial applications for frp panels is their use as skylights and sidelights by manufacturers of pre-engineered metal buildings. (Findings 36-44.) [22]

36. The pre-engineered metal building, which is basically made of corrugated steel, is well-accepted as an economical method of constructing manufacturing plants, warehouses, retail stores, small office buildings, schools, gymnasiums, and agricultural buildings. (CX's 288A-H; Tr. 522, 1054-55.)

37. Typically, a pre-engineered metal building manufacturer produces a package containing all the components and accessories of the building including primary framing members, wall and roof coverings. This package or "knockdown building" is distributed through franchised dealers who erect the building for the ultimate user. (Tr. 523, 1052-54.)

38. The pre-engineered metal building industry is substantial. In 1974, the 29 members of the Metal Building Manufacturers

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[22] As indicated in Finding 31 patio kits are sold by Sears in aluminum only. The prices of these kits (for standard 8 x 16 ft. patio) range from $114.95 for mill finish aluminum to $234.95 for white enamel finish aluminum. (CX 309-Z-72). A professionally custom installed patio cover costs approximately $3.75 per square foot for aluminum and up to $4.00 per square foot for frp, but in many cases the installed prices are the same for both materials (Tr. 1529, 1539) despite the fact that the cost of frp panels sold to custom installers is higher than the cost of aluminum. See note 20, *supra*.

Association (an association of pre-engineered metal building manufacturers accounting for approximately 75-80 percent of the market) had sales of $790 million. (CX 286A; Tr. 1064-65.)[23]

39. The basic covering materials used in pre-engineered metal buildings are corrugated steel panels. Corrugation imparts strength to the surface. (Tr. 524, 1052-53, 1078.)

40. Frp panels, most commonly corrugated eight ounce per square foot panels, are used in these corrugated metal buildings as the skylights or sidelights [23] which transmit natural light to the working area. (CX 289-Z-8; Tr. 457, 460, 713, 1058-61, 1223.)[24]

41. Because frp panels can be corrugated to the same specifications as steel, they easily "nest" with the steel corrugated panels and are installed in exactly the same manner as the steel skin of the pre-engineered building. Costly wooden frames or sashes are not required in order to install frp panels in corrugated metal buildings. (CX's 67C, E, 289-Z-8; Tr. 343-44, 455, 460, 524, 646, 713, 1058, 1175.)

42. Frp panels are the only materials used as skylights or sidelights in corrugated metal buildings.[25] It is the standard material for this purpose and there is no feasible substitute at this time. (Tr. 713, 953-55, 1060-64, 1080-81.) [24]

43. Manufacturers of frp panels do not consider the prices of glass, acrylic, polycarbonate, PVC or any other material in setting their prices for frp panels to be used for nesting in corrugated metal buildings. (Tr. 320-24, 471-72, 636-40, 715-16, 934-39, 1208.)

44. While frp panels are only a relatively small part of a corrugated metal building (Tr. 1052-53), the volume of sales by frp manufacturers to the pre-engineered metal building industry is substantial. In 1974, five frp panel manufacturers — Thorolyte, Idaho Chemicals, Lasco, Reichhold, and Glasteel — had sales of approximately $6.8 million to corrugated metal building manufac-

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[23] It has been estimated that pre-engineered metal buildings account for about 20 percent of the single-story non-residential construction in the United States. (CX's 288D, 289A-Z-17; Tr. 1077-78.) In addition to the pre-engineered metal buildings, there is a large volume of corrugated metal building construction done by custom builders. (Tr. 523-24, 1069-70.)

[24] Typically, such panels were being sold in 1977 for 50¢ per square foot. (Tr. 458.)

[25] Because glass cannot be corrugated it must be placed in a sash or a frame — in other words, glass does not naturally "nest" with corrugated steel panels. The substantially higher installed cost of glass as well as its breakability has meant that use of glass in industrial or commercial buildings is confined to showroom or office areas. Similarly, other materials such as acrylic and polycarbonate sheet not only are substantially more expensive than frp panels but in addition they are not available in corrugated form and require the high installation costs of sashes or frames. Polyvinyl chloride (PVC) has been tried in corrugated metal buildings and has been rejected for lack of chemical stability, tendency to warp or yellow, and its low level of structural integrity. (Tr. 357-59, 460-63, 645-47, 713-15, 953-55, 1057-61, 1660.)

turers. (Tr. 668, 683-84, 997, 1043, 1189, 1205, 1245, 1259, 1962, 1973.)[26] Prior to the Reichhold acquisition, Corrulux, too, sold panels to the same class of users. (CX's 56A-D; Tr. 712.)

"Liners"

45. Frp panels are used to line the interiors of truck trailers, railroad cars, and marine cargo containers. They are also used as liners in food processing plants and farm buildings. (CX's 21, 22, 122F, G; RX's 15, 17; Tr. 834-35, 844, 862-63.)

46. Frp panels used in the liner application are generally flat (but some are ribbed), opaque, and usually weigh above 12 ounces per square foot. (Tr. 833-34, 837.)

47. Frp panels possess several physical characteristics which make them particularly well-suited for use as liners in refrigerated trailers, railroad cars, as well as food processing plants. They are light (an important consideration to cargo carriers), [25] durable (and thus do not crack allowing the entry of bacteria), can be installed without seams (again, retarding the growth of bacteria) and provide an easily cleanable surface which is essential for the maintenance of high standards of sanitation. (CX's 21-22, 159, 174B, 176A, B; RX's 15, 17; Tr. 862-63.)

48. Other materials such as ordinary steel and aluminum are not as well-suited as frp panels for use as liners in refrigerated trailers or railroad cars. Steel has a tendency to rust and aluminum produces a black oxide[27] which could damage food products. (Tr. 868-69.)

49. Approximately 99 percent of newly built refrigerated truck trailers and refrigerated railroad cars are lined with frp panels. (Tr. 863-64, 867-68.)

50. Frp panels are also installed in trailers, moving vans, and railroad cars which are used for transporting non-food products. They are preferred for this general transportation application because they provide a surface that does not damage cargoes, resists the corrosive effects of acids,[28] and can withstand forklift damage. (Tr. 864-66.)

51. For the interior of food processing plants, the United States Department of Agriculture is encouraging the use of frp panels in place of porcelain enamel or stainless steel since the high-impact

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[26] See also Tr. 416 for evidence of sales of frp panels to corrugated metal building manufacturers by Filon. Also, in 1973 Resolite had sales of about $2 million to the pre-engineered metal building industry. (Tr. 456-57; Table III, *infra.*)

[27] While stainless steel will not rust, it is not used to line refrigerated truck trailers or railroad cars because its cost is considerably greater than frp panels. (Tr. 869.)

[28] An important consideration in transporting such corrosive products as batteries, salt, and leather. (Tr. 864-66.)

resistance and cleanability of the product tends to prevent [26] the collection of dirt and bacteria. (CX 114; RX's 18A, B; Tr. 1029-30.) As a result, many food processors are using frp panels in new construction and in refurbishing existing food plants. (Tr. 870, 1029-30.)

52. The "liner" segment of the industrial application of frp panels has become important. In 1974, the combined total of liner frp panels sold by just three companies — Kemlite, Molded Fiberglass, and Cincinnati Milacron — was approximately $15.5 million. (RX's 28E, 68; Tr. 909, 1285-86, 2019.) In addition, liner panels were produced by Kalwall, Glasteel, Ornyte, Reichhold, and Lasco. (Tr. 644, 1901-02.)

53. No producer of frp panels for the liner application takes into account the prices of ceramic tile, steel, aluminum or any other material in setting his price for frp panels. (Tr. 636-40, 878-79, 934-39.)

54. It is anticipated that the industrial applications for frp panels, particularly their use as liners, and as skylights and sidelights will be the area of the greatest future growth for this product. (Tr. 995, 1044, 1252-53.)

"Garage Doors"

55. Frp panels are used by manufacturers of garage doors. These garage doors are typically the sectional overhead variety in which the frp panels are installed in an aluminum frame. (Tr. 337.)

56. Other materials including steel, wood, fiberglass, and aluminum are used by manufacturers of garage doors. (Tr. 947, 1005.) There is some indication in the record of functional and price distinctions between these other materials and frp panels in the garage door application (particularly frp's light weight and ability to transmit natural light. (CX's 28, 309-Z-63; Tr. 337-39, 645, 947-49).) Complaint counsel's evidence, however, with respect to this application is [27] flimsy at best and they failed to prove that any differences which may exist among various materials used in the garage application are so substantial as to indicate a relevant market or submarket.

"Glazing Material"

57. Flat frp panels can be used as replacements for glass in window sashes in conventional buildings.[29] (See, *e.g.*, RX's 19A, B.)

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[29] Use of frp panels as window glazing — *i.e.*, as a replacement for glass or other materials in a sash — should not be confused with the "nesting" of frp panels as skylights or sidelights in pre-engineered industrial metal building in which no sash is required. (See Findings 40-42.)

Generally, frp panel manufacturers testified that use of flat panels as a glazing material — *i.e.,* as a replacement for glass in sashes — constitutes a minor part of their businesses. (Tr. 345, 555-56, 643-44, 955, 1044, 1971; but see Tr. 1924-25, for evidence that Reichhold has been able to sell substantial amounts of frp panels as replacement for entire glass systems including sashes.)

58. Thermoplastics, such as acrylics and polycarbonates, as well as glass itself, are by far the most widely used window replacement materials. (RX 2; Tr. 1622-23, 1635.) Because these other plastics are transparent and frp panels are not, frp panels are not an important glazing material even though they are less expensive than acrylics and polycarbonates. (CX 105; Tr. 1622-28, 1637-38, 1639-40, 1643-45, 1649, 1651-53, 1661-62.) Complaint counsel failed to prove that use of frp panel in the glazing application indicates a relevant market or submarket.

59. There are still other industrial applications for frp panels, such as their use as sign material and as "cladding" for water cooling towers[30] in which [28] they compete directly with acrylics, other plastics, asbestos cement, and wood. (RX's 18D, 36-37D; Tr. 419, 1905-08.) Complaint counsel's proof with respect to these applications is anecdotal and thus they failed to prove that use of frp panels in these applications indicates a relevant market or submarket.

The Greenhouse Application

60. The manufacture of commercial greenhouses is a substantial industry. In 1976, the dollar volume of sales of greenhouses to commercial growers was approximately $50 million. Of this total, 50 percent was derived from the sale of frp glazed greenhouses, 30 percent from the sale of polyethylene film greenhouses, and 20 percent from glass greenhouses. (Tr. 1095.) Sales of commercial greenhouses are usually made on a "turnkey" basis in which a complete, operating structure is built by the greenhouse manufacturer. To offset the cost of labor, a recent development has been the sale of do-it-yourself greenhouse kits which are assembled by the growers. (CX 64-o; Tr. 1703-04.)

61. In addition to commercial greenhouses, institutional greenhouses are constructed for universities and high schools which are mostly made of glass. Hobby greenhouses are made mostly of polyethylene film but glass and frp panels are also used by hobbyists. (Tr. 1096.)

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[30] See, CX 261B.

62. The basic frp panel sold to greenhouse manufacturers[31] is 50 inches wide by 22 feet long. Typically, the frp panels for the greenhouse application weigh four [29] ounces;[32] are coated with Tedlar;[33] and are made in a corrugated configuration. (Tr. 1098-99.)

63. Based upon total sales of 23.5 million square feet as reported by frp manufacturers to the Fiberglass Reinforced Panel Council, total sales by frp panel manufacturers to the greenhouse trade was approximately $6.6 million in 1974. (CX 57-o.)[34]

64. The installed costs of the three basic glazing materials used in commercial greenhouses vary substantially. Frp panels, which are relatively easy to install, are sold on the basis of an installed cost of $1.65 per square foot as compared to $1.90 per square foot for glass which requires an expensive glazing operation. The installed cost of polyethylene film is approximately $1.00 per square foot. (CX 64W; Tr. 340-41, 1101-02.)[35] [30]

65. The following are the physical characteristics of frp panels, glass, and polyethylene film which are relevant to the greenhouse application:

(a) Frp panels have a fairly long life-span before darkening (about 25 years if Tedlar coated), high resistance to hail but are inflammable.[36] They transmit diffused light,[37] but their translucency also means that they cannot be double-glazed for fuel-conservation purposes. (CX's 35, 64i, W, X, 65, 67E, 68B, 184; RX's 11C, 12C, D; Tr. 464-68, 1101, 1704-05, 1710.)

(b) Glass has an indefinite life-span. A glass panel is susceptible to hail damage, but presents no fire hazard. Glass panels give clear undiffused light which is important in geographic areas of low light intensity. (Tr. 466, 1118, 1710, 1748.)

(c) Polyethylene film has a short life-span (one to three years) but it can be removed easily to allow exposure for the purpose of hardening the flowers. Polyethylene film, which is transparent, can be double-glazed thus creating an air space between the layers which serves to [31] conserve energy.[38] Seasonal removal, however, of a double-layered polyethylene film greenhouse would not be feasible. (RX's 9, 12i; Tr. 466-67, 1116, 1704, 1788-89.)

66. The physical characteristics of the three principal greenhouse materials, as well as the installed cost differences described earlier,

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[31] Frp panel producers sell to greenhouse manufacturers, greenhouse equipment distributors, and directly to nurseries. (Tr. 1129, 1142, 1905.)

[32] Five ounce panels are also used in the greenhouse application. (Tr. 457, 1098.)

[33] "Tedlar" is a du Pont polyvinyl fluoride film that retards discoloration and loss of light transmission. (CX's 64T, U; Tr. 331, 367-68.)

[34] In 1974, the Tedlar-coated four ounce panels used widely in the greenhouse trade sold for approximately 28¢ per square foot; that is, 19¢ for the panel, 9¢ for the coating. (Tr. 979, 1966.)

[35] The leading greenhouse manufacturer sells four ounce Tedlar-coated frp panels for 40¢ per square foot, glass for 36¢ per square foot, and polyethylene film for 1¢ per square foot. (CX 64-Z-1, Z-4, Z-6.) This manufacturer pays approximately the same price, 22¢ to 25¢ per square foot, for glass and frp panels. (Tr. 1099.)

[36] With special treatment, frp panels can be made fire resistent. (CX 64i; RX 11B but see CX's 65G, H.)

[37] Diffused light not only reduces burning and spotting of plants (see Finding 67) but also creates a larger growing area. (Tr. 464.)

[38] A double-layer of polyethylene film allows 92.4 percent of the light transmission of glass. (RX 9.)

have created historical preferences for each material depending upon the crop grown and the geographic area where the crop is grown. Thus Roper-IBG, the largest commercial greenhouse manufacturer in the United States,[39] which sells greenhouses made of all three covering materials, experienced the following sales pattern in 1976: [32]

TABLE 2: ROPER-IBG 1976 SALES OF FRP, GLASS, AND POLYETHYLENE BY CROP AND AREA AS PERCENT OF TOTAL SALES OF $8.5 MILLION

	Northwest	*Northeast*	*Southwest*	*Southeast*	*Total*
Cut Flowers					
FG (frp panels)	3%	0	19%	2%	24%
Glass	2%	0	09%	0	2%
Poly	0	0	0	0	0
Potted Plants					
FG	0	0	23%	3%	26%
Glass	0	2%	0	0	2%
Poly	0	0	0	0	0
Bedding Plants					
FG	0	0	0	0	0
Glass	0	0	0	0	0
Poly	1%	15%	3%	1%	20%
Foliage Plants					
FG	2%	0	4%	8%	14%
Glass	0	0	0	0	0
Poly	0	0	0	2%	2%
Vegetables					
FG	0	0	8%	0	8%
Glass	0	0	0	0	0
Poly	0	2%	0	0	2%

Source: (CX 66)

[33] 67. As shown in Finding 66, cut flower growers, the most important greenhouse growers (CX 65B), prefer frp covered greenhouses.[40] The geographic centers for the cultivation of cut flowers are in the Salinas Valley area of California, and in the Denver, Colorado area. Since these are areas of high-intensity light which could cause burning and spotting of the flowers if the light were not diffused, the light-diffusing quality of frp panels is preferred. (CX 65D; Tr. 341, 465-66, 950, 1104-06, 1119.) In addition, light diffusion has been

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[39] Roper-IBG has about 17 percent of the greenhouse market. (Tr. 1095, 1097.)

[40] The preference appears to be particularly strong among growers of carnations, chrysanthemums, and southern growers of roses, but it is not as strong with northern producers of roses, who require more intense light transmission. (Tr. 466, 1119.)

found to stimulate stem and lower leaf growth, thus producing larger blooms. (Tr. 1104.)

68. Growers of potted plants[41] are more geographically dispersed than the cut flower growers. Potted plants are difficult to ship and growers tend to be located near large urban population centers irrespective of climatic conditions. Climatic conditions, however, tend to dictate the material used in constructing a greenhouse for potted plant cultivation. As a result, in low intensity light areas such as the Northeast or Northcentral glass is favored, but in southern and western areas where there is high intensity light, frp greenhouses are favored. (CX 65D; Tr. 465, 1106-07, 1781.)

69. Bedding plants[42] are widely grown all across the country but are usually cultivated by smaller growers. The cultivation of bedding plants tends to be a short-term operation confined to the early part of the year. Accordingly, bedding plant growers prefer [34] to use the temporary covering of polyethylene film which can be removed easily for hardening of the plants. (CX's 65D, E, 66; RX 9; Tr. 1107-08, 1126-27.)

70. Foliage plants for indoor decoration are mainly grown in the high intensity light areas of Florida and California. As in the case of cut flowers, frp panels are favored for their light diffusion quality. (Tr. 1108-09, 1760-61.)

71. The experience of Roper-IBG has been that vegetable growers who use greenhouses[43] (a very small segment of the greenhouse market) favor frp greenhouses. (CX's 65E, 66.)

72. As the market for various kinds of flowers changes so does the market for the various greenhouse coverings. To illustrate, because of the recent massive importation of cut flowers from Latin America (Columbia) domestic cut flower growers have limited their expansion with the result that there has been a decline in new frp greenhouse construction by cut flower growers. (CX's 65A, B; Tr. 1109, 1746.)[44] On the other hand, the sharp increase in the popularity of foliage plants has resulted in an equally sharp increase in the demand for frp panels by the growers of these crops. (Tr. 1127, 1760-61.) Similarly, the boom in the bedding plant market and the sharp increase in energy costs in the northern parts of the country, where many bedding plants growers are located, have increased the demand for double-layered polyethylene film. (CX 66; RX's 9, 10; Tr. 1109-10, 1120-21, 1127, 1750-51.) [35]

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[41] Lillies, poinsettias, and geraniums, for example. (Tr. 1103.)

[42] Carnations, petunias, and gloxinia, for example. (Tr. 1103, 1747.)

[43] Predominantly tomato growers. (Tr. 1103.)

[44] There are indications, however, that bad weather, disease, and import quotas may combine to limit severely the lasting impact of this invasion. (CX 65C.)

73. The consumption patterns described above, reflecting the area in which the grower is located and the crop produced, are not immutable. (Tr. 1747–48.) The traditional installed cost advantage of frp panels has recently been challenged by the importation of the so-called "Dutch Greenhouses" from the Netherlands. On occasion, these glass greenhouse imports have undersold frp panel greenhouses in geographic areas which have traditionally been considered frp panel strongholds. (Tr. 1706–09, 1715.) Even polyethylene film, which in a double-layer application can conserve fuel, may become a feasible alternative to the traditional uses of frp if the cost of energy exceeds the cost of replacing relatively short-lived film.[45] This threat is less likely to emerge in the warm growing areas in the Southwest and Florida where energy costs are not a major factor. (Tr. 1120–21.)

74. While these threats to the historical frp preference must be recognized, especially in a changing flower industry in which large commercial growers and the use of cost analysis are becoming more evident (Tr. 1711–13, 1714), it would be a distortion of current trade realities to conclude that the emerging challenges are more significant than the established patterns. The preference of many growers for frp is not a fly-by-night phenomenon. It has developed over a nearly twenty year period,[46] to the point that despite the importation of some glass greenhouses, there has not been a significant number of glass greenhouses [36] installed by cut flower growers within the past six years. (Tr. 1105, 1124–25.) Moreover, the record shows that the three greenhouse materials are still largely price insensitive to each other. For example, a 5 percent increase in the cost of frp panels would not cause greenhouse buyers to shift their purchases from frp panels to glass. (Tr. 1117.) Similarly, a price change in polyethylene film does not affect frp panel sales. (Tr. 413, 660.) And it has been estimated that the price of frp panels would have to go up more than 10 percent to cause frp panel greenhouse purchasers to shift to polyethylene film, and some cut flower growers probably would not change from frp panels to glass even if glass were cheaper. (Tr. 1118–19, 1125.)

75. Most important, the current preference for frp in the greenhouse application is such that frp panel manufacturers simply do not take into account the prices of glass or polyethylene film in setting their prices for frp panels. (Tr. 323, 413–14, 471–72, 561, 589, 636–40, 659–60, 934–39, 1208, 1227–28.)

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[45] Double-layered polyethylene can save 40 percent on heating cost as compared to a single wall system. (RX 9.) Since 1973 the cost of energy used by growers in the Northeast has increased 250 percent. It now comprises 30 percent to 35 percent of a grower's operating cost in the northcentral and eastern portion of the country. (Tr. 1116–17.)

[46] See CX 65A; Tr. 1700–01.

Supply-Side Perception of Competition

76. Apart from the industrial application for skylights and sidelights and as liners for refrigerated cars where no reasonable alternatives are available, there clearly are alternatives to frp panels in their other key applications as shown in Findings 24-34, 55-75. What the record shows, however, is that the different physical characteristics of frp and aluminum in the patio field, as well as the physical characteristics and costs of frp panels as compared to glass or polyethylene film in the greenhouse application, have established a preference for frp panels among a large number of users who want low cost installation, light transmission, light diffusion and the other qualities of frp panels. (See Findings 24-34, 60-75.) Not only is this preference measurable (total frp sales are not insubstantial) but the frp panel producers function competitively as if the contest to fulfill this preference was indeed a commercially recognizable market. (Findings 77-87.) [37]

Distinct Prices and Price Sensitivity

77. Producers of frp testified overwhelmingly that their competition comes solely from other frp producers. The frp producers said (1) that they do compete against other frp panel producers, and (2) that they do not compete against producers of aluminum, glass, polyethylene film, ceramics, pvc, wood, steel, acrylic, polycarbonate, or any other material. (Tr. 320-24, 336, 469, 471-72, 542-48, 560-62, 632, 636-40, 659-60, 715-16, 878-79, 934-39, 1208, 1223-24, 1260.)

78. In setting their prices for frp panels, the *only* prices which frp producers take into account are the prices of other frp producers. (Tr. 320-24, 469-72, 542-48, 615-16, 636-40, 659-60, 715-16, 878-79, 934-39, 1208.)

79. The frp panel producers neither consider nor monitor the prices of other materials. (Tr. 320-24, 469-72, 542-48, 582-83, 615-16, 636-40, 659-60, 715-16, 878-79, 934-39, 1208, 1227-28, 1232.)

80. The prices charged for frp panels are not sensitive to changes in either the demand or the prices of other materials. (Tr. 320-24, 336, 413-14, 469-72, 542-48, 582-83, 615-16, 636-40, 659-60, 715-16, 878-79, 934-39, 1208, 1227-28.)

Recognition of an Frp Panel Industry

81. For the most part, frp panel producers treat frp panel production as a distinct business: that is, they only manufacture frp panels or produce frp panels in a separate part of multi-product

firms. (CX 122F; RX 89, p. 4; Tr. 307-09, 454-55, 534, 710, 832-33, 923, 1141, 1185, 1234, 1247-48, 1891.)[47] For example, [38] Reichhold's frp panel business is conducted through its Reinforced Plastics Division which only sells frp panels and the accessories used to install frp panels. (Admissions 1, 2, 3, CX's 305B, M; Tr. 1891.)

82. Frp producers such as Reichhold, Filon and Resolite refer to an frp "industry" in their promotional literature. (CX's 36C, 215, 258D; Tr. 324, 477-78.) See also CX's 304A and 311M, N for recognition of a "Fiberglass Reinforced Panel Industry."

83. The main frp panel producers have joined together to form an association of producers and suppliers who have common marketing and technical concerns. (See Findings 84-87.)

84. The Society of the Plastics Industry (SPI), which has over 1,000 members, is the major plastics trade association in the United States. Within SPI there is a Reinforced Plastics Composites Institute which carries out various technical and promotional activities on all reinforced plastics. The Fiberglass Reinforced Panel Council, a subsection of the Reinforced Plastics Composites Institute was formed over 25 years ago "To bring about the establishment of a stable and integrated growth into the Fiberglass Reinforced Panel Industry" and "to advance the best interest of the. . . Fiberglass Reinforced Panel Industry." (CX 304A.) The membership of the Fiberglass Reinforced Panel Council is composed solely of manufacturers of frp panels who use the continuous line process and their suppliers. With the exception of Kemlite,[48] all of the significant manufacturers of frp panels are members of the Fiberglass [39] Reinforced Panel Council. The Council, which holds three meetings each year, has its own by-laws, elects its own officers, administers its own business affairs, and appoints its own committees to carry out special projects. (Admissions 42, 43, 44, CX's 305F, N; CX's 304A-C; Tr. 225-28, 230-32, 241, 325, 472-73, 548-49, 650-51, 720, 939-42, 1989.)

85. The Fiberglass Reinforced Panel Council collects frp panel sales data from eight major manufacturer-members and disseminates this information to its membership in quarterly reports. (CX's 57A-o; Tr. 233-34.)

86. The Fiberglass Reinforced Panel Council has taken the initiative in promulgating a voluntary product quality standard for frp panels. The standard, P.S. 53-72 "Glass Fiber Reinforced

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[47] But see Tr. 627 for exception in case of Lasco; Lasco, however, has a separate frp panel sales force.

[48] Kemlite left the Council in 1965 to concentrate its efforts on transportation industry associations in which it could promote its liner panels. (Tr. 848.)

Polyester Structural Plastic Panels" which covers five, six, and eight ounce panels,[49] was published by the National Bureau of Public Standards, U.S. Department of Commerce in April 1972. All significant manufacturers of frp panels have accepted this voluntary product standard and many use it in promoting their products. (Admission 49, CX's 305G, N; CX 190; Tr. 232-33, 326-27, 473, 549, 650-51, 941-42.)

87. In addition, the Fiberglass Reinforced Panel Council has engaged in such activities on behalf of frp panels manufacturers as performance testing, the publication of technical information about frp panels, the monitoring of building codes to anticipate their potential effects on frp producers and the covening of meetings to discuss marketplace trends. (Admissions 52, 53, CX's 305G, H, N; CX's 57, 194; Tr. 225-27, 235-40.) [40]

Specialized Vendors

88. Frp panels, like aluminum panels, glass, or polyethylene film, are distributed through mass merchandisers, distributors, and original equipment manufacturers. The customers of frp manufacturers who buy frp for the patio application (mass merchandisers and distributors to lumberyards and custom awning fabricators) also buy aluminum panels for use in the patio application. Similarly, the same greenhouse manufacturers who buy frp panels also buy glass, and polyethylene film for use as greenhouse covering. Distributors of industrial glazing materials simultaneously handle frp panels, acrylics, and polycarbonates. (RX's 4-7, 11A-12J, 53, 73B; Tr. 509-10, 1525, 1582, 1622-23, 1702-03.) The only exceptions to this pattern — that is, *no* specialized vendors of frp panels — are the manufacturers of pre-engineered metal buildings and refrigerated vans who apparently use no material other than frp panels for the skylighting and refrigerated car liner applications. (See Findings 42, 49.)

Conclusion on Market Definition

89. On the basis of buyer preference for frp panels in certain applications, which derives from the physical characteristics and cost of the material, as well as the suppliers' perception of competition, I have concluded that the production of frp panels represents a relevant market or "line of commerce." (Findings 14-88.)

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[49] A four ounce panel standard has been under consideration by the Council for many years. (Tr. 942, 1990-91.)

MARKET STRUCTURE AND ENTRY

Concentration

90. In assembling its proposed frp panel universe, complaint counsel argue for exclusion of Butler Manufacturing Company, an important manufacturer of pre-engineered metal industrial buildings. Butler's [41] production of frp panels is for "captive" use only as skylights and sidelights in its own steel buildings. (Tr. 1484-87, 1495.)[50] Butler's production is not sold in the merchant market and Butler has no intention of entering the merchant market. (RX's 25A, C, *in camera;* Tr. 349, 541-42, 634-35, 718-19, 1066-67, 1484-87, 1497, 1500-02, 1508, 1519.) Inclusion of Butler in an frp panel universe would tend to distort an assessment of potential anticompetitive effects which depend upon market structure and concentration ratios since the record shows overwhelmingly that frp producers do *not* consider Butler to be a competitor, and Butler is so far removed from considering itself in competition with frp panel producers that it knows little about the prices of these producers. (RX 25A, C, *in camera;* Tr. 349, 541-42, 634-35, 718-19, 1508.)

91. With the exclusion of Butler's captive production, the frp panel universe appears as follows: [42]

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[50] Butler produces and sells a small amount of replacement panels for its pre-engineered metal buildings. (RX 26B.) Since the panels produced by other manufacturers are not compatible with Butler's components, purchases of non-Butler replacements by owners of Butler buildings are rare. (CX 25C, *in camera;* Tr. 1503-04.)

TABLE 3; MARKET SHARES OF FRP PRODUCERS, 1972-1973; 1973 RESTATED TO SHOW EFFECTS OF ACQUISITION

	1972			1973			1973 Restated		
Name of Manufacturer	Rank	Dollar Sales	Percentage Share of Total Dollar Sales	Rank	Dollar Sales	Percentage Share of Total Dollar Sales	Rank	Dollar Sales	Percentage Share of Total Dollar Sales
Reichhold Chemicals, Inc.	3	8,629,690	16.61	2	11,916,853	18.85	1	14,727,038	23.30
Vistron Corp. (Filon Division)	1	11,649,795	22.42	1	12,710,000	20.11	2	12,710,000	20.11
Lasco Industries, Inc.	2	8,700,170	16.74	3	11,110,029	17.57	3	11,110,029	17.57
Kemlite Corporation	4	6,402,719	12.32	4	7,775,333	12.30	4	7,775,333	12.30
Berdon, Inc. (Ornyte Division)	5	3,493,540	6.72	5	4,451,736	7.04	5	4,451,736	7.04
Glasteel, Inc.	10	1,321,309	2.54	6	2,905,892	4.60	6	2,905,892	4.60
Barclay Industries, Inc.	8	2,283,149	4.39	8	2,744,545	4.34	7	2,744,545	4.34
H. H. Robertson Co. (Resolite Division)	7	2,726,345	5.25	9	2,272,834	3.60	8	2,272,834	3.60
Molded Fiberglass Co.	9	1,970,709	3.79	10	2,209,306	3.49	9	2,209,306	3.49
Cincinnati Milacron	11	1,018,000	1.96	11	1,058,000	1.67	10	1,058,000	1.67
Fiber Glass Plastics, Inc.	12	377,920	0.73	12	441,534	0.70	11	441,534	0.70
Thorolyte Fiberglas, Inc.	13	371,506	0.71	13	420,992	0.67	12	420,992	0.67
Idaho Chemical Industries, Inc.	14	268,570	0.52	14	309,572	0.49	13	309,572	0.49
Kalwall Corp.	-	-0-	-0-	15	80,000	0.13	14	80,000	0.13
Corrulux Corp.	6	2,745,579	5.28	7	2,810,185	4.45	-		
Total of All Manufacturers		51,959,001	100.00		63,216,811	100.00		63,216,811	100.00
Total of Top Four Manufacturers		35,382,374	68.10		43,512,215	68.83		46,322,400	73.28
Total of Top Eight Manufacturers		46,630,987	89.75		56,424,573	89.26		58,697,407	92.85

Source: CX 302 except as follows: Kemlite (CX 307B, in camera); Molded Fiberglass (RX 27; Tr. 1318); Cincinnati Milacron (RX 68); and Kalwall (RX 83, p. 28).

[43] 92. Table 3 includes a Kemlite liner panel consisting of a sheet of plywood to which a layer of frp is bonded. (See RX's 30–32B.) Table 3 does *not* include the "sandwich" panels produced by Lunn Laminates which consists of two frp skins enclosing a plywood or urethane core. Lunn's products are *not* intended as liners — they are used as the entire sidewall of a truck trailer. (RX's 21A–H; Tr. 1382, 1393–94.) Lunn does not consider itself to be in competition with any firm in the frp panel business and no frp panel producer testified that it competes directly with Lunn, and most never heard of it. (Tr. 318, 475, 541, 634, 719, 1207, 1261, 1382–83.) The Lunn product sells between $1.50 to $2.00 per square foot as compared to about 50¢ to 65¢ for frp liner panels.[51] (RX 83, p. 61; Tr. 853, 905, 1405–06, 2019.)

Since Table 3 is confined to pre-acquisition sales it necessarily excludes the "sandwich" panels which were first sold by Kalwall in commercially significant quantities during the period 1975–1977 and which now constitute the largest part of Kalwall's business. Even if Table 3 had included these post-acquisition years, production of this product is not properly part of the frp panel universe. The Kalwall "sandwich" product consists of two frp facings and a grid core constructed of structural aluminum I-Beams. (CX 158B; RX 83, pp. 5–6, 51–52.) This product is not a liner: it is intended to be used to build the entire wall or roof of a building. (CX's 158B, C; RX 83, pp. 6, 45–47.) Kalwall's sandwich panels are produced on a [44] custom basis and most often are sold with installation included. (RX 83, pp. 14, 33, 48.) The Kalwall "sandwich" panels alone (that is, excluding cost of installation) cost between $4.50 to $12.00 per square foot. (RX 83, p. 49.) Table 3 *does* include Kalwall's 1973 sales of non-sandwich frp panels for the merchant market (RX 83, p. 28), but does not include such sales for the post-acquisition years 1974–1976. The officers of Kalwall made it plain that their principal product — a high technology "sandwich" panel — is not part of the frp industry, (CX's 157A, B; RX 83, pp. 55–56), and a producer of frp panels for the liner application does not consider the Kalwall "sandwich" a competitive product. (Tr. 912–14.)

Table 3 also excludes the production of M.C. Gill, a producer of high-engineered, custom-designed, and FAA-approved laminates for the aircraft industry which sell at prices as high as $8.00 per square foot. (Tr. 1434–37, 1449–50, 1452, 1456–60, 1465–67.) The head of marketing for M.C. Gill does not consider himself part of the frp industry and he does not compete with frp panel producers. Frp panel producers, including one producer who was located six miles away from the M.C. Gill plant, never heard of the firm. (Tr. 475, 540-41, 634, 719, 1002-03, 1434, 1458-60, 1464-65, 1469-70.)

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[51] Frp coated plywood panels which are used in the liner application, and which are included in Kemlite's sales as reported in Table 3, sell at a price of about 75¢ per square foot. (Tr. 854.) Kemlite also produces ribbed panels for the liner application which are priced at 77¢ per square foot. These ribbed panels are included in Table 3. (Tr. 853.)

Entry

93. There are no significant capital barriers to entry into the frp market.[52] [45]

94. There is no evidence that advertising is a significant entry barrier in this industry, although point of purchase advertising is a factor in selecting a supplier of frp panels. (Tr. 1920.)

95. There are no patent barriers to entry into the frp panel industry. (CX 3F; Tr. 378-79, 491-92, 611-12, 1197-98, 2031-32.)

96. Complaint counsel failed to prove that technical expertise was a significant entry barrier in the frp panel industry. While the chemical know-how required in frp panel production is considered complicated (Tr. 648-49, 1728) the weight of the evidence is that the technical expertise necessary for handling resins is readily available from resin producers. (Tr. 492-93, 612-13, 1198-1200, 2035.) Complaint counsel also make much of the fact that a continuous line consists of various pieces of machinery produced by different manufacturers and that no company produces or sells the entire continuous line as a package. (Admissions 31, 32, CX's 305E, N; Tr. 312, 486, 537-38, 572, 629, 928-29.) Although the continuous line must be designed and assembled by the frp panel producer himself, it is a relatively uncomplicated engineering process and it is common practice in the industry to hire a qualified engineer from another manufacturer, or to retain a consultant who can offer a "turnkey" construction contract. (CX's 3F, G, 311; RX's 14A-D, 43; Tr. 230-31, 355, 378, 612, 960-61, 1019, 1238, 1726.)

97. A new entrant into the frp panel industry, however, may be deterred by the prospect of competing against Reichhold and the Filon Division of Vistron, a subsidiary of Standard Oil of Ohio. These large corporations, which already control close to 45 percent of the market (see Finding 91), also have a competitive advantage because of their captive source of polyester [46] resin.[53] (Tr. 351-56, 564-65, 648, 860-61, 966-67, 971-72, 1168-69, 1213-14, 1257-58.)

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[52] Current replacement costs for a continuous process machine range between $30,000 to $700,000 depending on the degree of automation and the quality of the control systems desired. (CX's 3H, 136H, 312A; RX 25E, *in camera;* Tr. 517, 520, 613-14, 885, 959-60, 963, 1185, 1239.)

[53] Reichhold, for example, transfers resin to its Reinforced Panel Division at cost plus freight, which is below the market price. Reichhold is willing to forego its profit on the sale of resin and realize the profit, instead, on the sale of finished panels. Other raw material used by Reichhold in frp panel manufacture are transferred internally on the same basis. (Tr. 2032-33, 2064-66.)

In addition to the price advantage, integration can mean an assured source of supply. During the period 1973-74, frp panel manufacturers experienced a severe shortage of polyester resin caused by the oil boycott. As a result

(Continued)

98. Beginning in the late 1950's and early 1960's, there were a large number of firms which left the frp industry. These exits were attributable to the conversion by many firms to the continuous method process, which meant that small producers then using the hand lay-up method and without adequate resources to make the conversion, were no longer competitively viable. (Tr. 490-91, 494, 900-03, 967-68, 1025-26.) [47]

99. In the last ten years, there has been only one new entrant into the frp market, the Kalwall Corporation. (RX 25D, *in camera;* Tr. 967.)

100. In addition to the acquisition of Corrulux, Reichhold has acquired two other producers of frp panels — Alsynite (Reichhold's San Diego plant) in 1960 and Structoglas (Reichhold's Grand Junction plant) in 1965.[54] (Admissions 12, 14, 15, CX's 305C, M; CX's 13C, D.)

101. There is a trend in the frp panel market toward the acquisition of independent frp panel manufacturers by large firms: Alsynite, Structoglas, and Corrulux were acquired by Reichhold; Resolite was acquired by H. H. Robertson; Filon was acquired by Standard Oil of Ohio; and Lasco was acquired by Phillips Industries. (CX's 13C, D; Tr. 306-07, 454, 626, 860.)

EFFECTS OF THE ACQUISITION

102. The effect of Reichhold's acquisition of Corrulux may be substantially to lessen competition or tend to create a monopoly in the manufacture and sale of frp panels. (Findings 103-109.) [48]

103. In 1973, the pre-acquisition year, Reichhold ranked second in the frp panel market with 18.85 percent of sales and Corrulux ranked seventh with 4.45 percent of sales. The acquisition of Corrulux raised Reichhold's standing to first, and its market share to 23.3 percent. (See Finding 91.)

104. The acquisition directly increased the level of four firm concentration from 68.83 percent to 73.28 percent, and eight firm concentration from 89.26 percent to 92.85 percent. (See Finding 91.)

105. Corrulux was recognized by other frp panel producers,

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of this shortage, the industry's polyester resin needs could not be met. (Tr. 580, 2033.) Reichhold, however, usually has the capability of producing internally its requirements of polyester resin. (Admissions 4, 5, CX's 305B, M; see also Tr. 353.) Filon did not have an adequate internal supply of resin in 1973-74 (Tr. 428-29), but the company increased its polyester resin capability with the competition of a Covington, Kentucky plant in late 1973. (Tr. 405-06.) Resolite, too, receives at least part of its resin requirements from an integrated source of supply. (Tr. 478.) Uncertainty about resin supply was the reason Simpson sold Corrulux to Reichhold. (Tr. 820.)

[54] Structoglas, which had sales of about $3 million, was recognized as a significant competitor and may have ranked within the top five companies in the industry. (Tr. 351, 487, 563, 862, 970-71.) Alsynite, too, ranked near the top five. (Tr. 487, 562-63, 861-62, 969-70.) Structoglas was a division of a manufacturer of melamine dinnerware and toys ("Brookpark") which was in dire financial straits. Structoglas was acquired as payment for a debt owed Reichhold by Brookpark on a purchase of melamine. (CX 13C; Tr. 1890.)

including Reichhold, as a competitor during the Simpson years. (Tr. 575, 632, 665, 932, 972.) Prior to the acquisition Reichhold and Simpson solicited and sold to the same customers. (CX's 303, 310, 312; Tr. 972, 1070–72; see also Finding 44.) Simpson considered Reichhold one of his principal competitors. (Tr. 715–16.)

106. As a result of Reichhold's acquisition of Corrulux, actual competition between the second and seventh ranked sellers of frp panels has been eliminated. (See Findings 103, 105.)

107. As a result of the acquisition, competition between Corrulux and other frp panel producers has been eliminated. (See Finding 105.)

108. Respondent has acquired three significant firms in the frp panel market. (See Finding 100.) If this latest acquisition were to be approved, it may tend to trigger an increase in merger activity in the frp panel market since Reichhold's principal competitors may seek approval for acquiring similar market shares.

109. As a result of the acquisition, barriers to entry into the frp panel market have increased. A potential entrant, examining the post-acquisition [49] market shares of 43 percent for the two largest firms, may be deterred from entering because of uncertainty as to its ability to obtain a large enough market share in a relatively small total market. (See Finding 97.)

MARKET CONDITIONS

110. Given the structure of the frp panel industry and the increase in concentration which resulted when Corrulux was acquired, this horizontal acquisition is at least presumptively illegal. According to respondent, however, there are market conditions in the frp panel industry which assure that price competition will remain vigorous, whatever the level of concentration. In Part III, below, I have said that this argument misconceives the purpose of Section 7 which is intended to eliminate the growth or perpetuation of anticompetitive market structures that *may* substantially lessen competition irrespective of the existence of some other pro-competitive aspects of an industry. Moreover, as Findings 111–115 below show, the market conditions cited by respondent are not so inevitably pro-competitive as to excuse a permanent structural change which results when an actual competitor is eliminated.

111. Competition in the frp panel industry is in terms of price, quality, and service. (Tr. 977–78, 985–86, 1188, 1245.) Some important users do not believe that the products of all producers are interchangeable, and a reputation for quality can be a crucial consideration in selecting a supplier. In the greenhouse application,

for example, price is not always a primary consideration, and if a supplier has a proven record for quality, only at a 10 percent differential would a leading greenhouse manufacturer even begin to start looking at an alternative supplier. (Tr. 1730–31, see also CX's 65F, G.) While price is very important in the sale of staple products such as four ounce corrugated patio and greenhouse panels, it would take a not insubstantial price difference — a 1/2¢ to 2¢ differential on products which sell below 20¢ per square foot — [50] to induce a switch from a supplier of proven quality and service to another unproven manufacturer. (Tr. 977, 980, 1146–48, 1188, 1192–93, 1544, 1921.) Moreover, despite the claimed vigor of price competition, some producers seem to be able to charge prices which are considerably above the level of their competitors. To illustrate, for the four ounce panel, Idaho Chemical and Thorolyte charged 19¢ recently (Tr. 1224–25, 1243) as compared to about 15¢ charged by Filon, Barclay, and Glasteel. (Tr. 437, 578, 957.) As for the heavier eight ounce panels, Resolite sets its prices at 50¢ (Tr. 458) while Glasteel's price is 40¢. (Tr. 1040.)

112. From the early 1960's to 1973 there was a gradual decline in average frp panel prices, although the decline was by no means constant and there were periods when prices rose. (CX 314; RX's 38H, 39.) This overall decline is mainly attributable to a sharp reduction in the cost of resin and the production of lighter panels as well as the introduction of the continuous line process and its attendant savings in raw material and labor costs. (Tr. 392, 572–73, 897–98, 903–04, 1180–82, 1243–44.) Prices went up precipitously in 1974 reflecting the rise in the cost of oil-based resins; there was a decline in prices from the 1974 high's during the recession and post-recession period of 1975–1976; and at the time of the hearings herein selective prices were increasing again. (CX 314; RX 39; Tr. 392–94, 428–29, 579–80, 609–10, 1145, 1215–16, 1243–44.)

113. The conversion to the continuous line process in the 1950's and 1960's resulted in a substantial increase in frp panel manufacturing capacity. This in turn has meant that during most of the period from the 1960's to the present the industry has had overcapacity. (RX's 38H, 89, pp. 6, 13–14; Tr. 500, 504–05, 595, 1182, 1732.) Unused capacity, however, is to some extent a [51] function of the seasonal nature of the business since production is usually concentrated within the period April to September. (Tr. 594–95, 1036, 1068, 1183–84, 1259, 1551, 2018.) It should also be noted that there have been periods when the entire industry has operated at close to full capacity. Thus in the period late-1973 to mid-1974, almost all plants were operating either at or near full capacity or at the highest level

of production compatible with adequate maintenance, the supply of resin, and the availability of technical personnel. (CX 17A; Tr. 504-05, 580, 592–94, 974, 1728–29, 2036–37.) Moreover, there are indications that underutilization of capacity will diminish as the business recovery from the deep 1974–1975 recession continues. Reichhold's two continuous lines at Grand Junction are presently operating near full capacity and respondent is contemplating adding still additional capacity. (Tr. 2057–58.) One of Filon's plants was closed during the recession and has not yet been reopened, (see, however, Tr. 431 for an indication that soon it will reopen) but the other is now operating at full capacity. (Tr. 400–02, 433.) Glasteel, which was operating its plant in 1976 at 80 percent of maximum feasible capacity, is actively considering construction of another plant. (Tr. 1039–40.) See also Tr. 595, 2017–18.

114. While several manufacturers testified that unused capacity has led to price competition (Tr. 380, 496–97, 1970, 2038–39) there is no evidence of *actual* over-production which may have served as a severe price-depressant. To the contrary, producers seem to operate on the basis that excess capacity is simply taken out of production since the cost of maintaining unused equipment is low. (RX 89, pp. 13–14; Tr. 397–98, 1969; see also Tr. 1517–18.)[55] [52]

115. In the recession and post-recession years of 1974 to 1976 profits of some frp producers have been low, and Reichhold has operated at a loss. (RX's 42A, B, 44, 88, *in camera;* Tr. 1143–44, 1684, 2037.) Low or no profits resulted from a combination of price competition, the recessionary decline in demand for light corrugated frp panels used in the residential and greenhouse segments of the markets, and the increase in raw material costs. (CX's 65A, 286A, B, F; Tr. 413, 427–29, 437–38, 1028–29, 1065–66, 1164–65; but see Tr. 1037–38 for evidence of an upward trend in profits at Glasteel on the sale of residential and greenhouse panels.)[56] Margins on the sale of heavier industrial panels have been higher than the returns on the more competitive light, corrugated panels and producers of these heavier products have experienced a favorable level of profit. (CX's 122D, R; Tr. 871, 906–07, 1028–29, 1039, 1161–62, 1254–55, 1922.)

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[55] The major unit cost involved in frp production is raw material. Thus in 1972, even before the sharp rise in resin prices, raw material costs were estimated at 8.25¢ per square foot as compared to 3/4¢ for direct labor. (RX 14B.)

[56] Low profits may also reflect a particular company's objectives. Idaho Chemical's profits ranged from $1,000 to $13,000 in the years 1974 to 1976. With respect to profits, the head of the company testified "we try not to make any." (Tr. 1211–12.) The company apparently operates on the philosophy of adequate compensation for executives, liberal vacations, bonuses for everyone, and contributions to a trust fund for employees. (Tr. 1211–12.)

THE CONDITION OF CORRULUX

116. At the time of the Reichhold acquisition in 1974, Corrulux was a small, struggling, but viable company. (Findings 117-132.)

117. Simpson had previously acquired Corrulux in December 1971 from the Johns-Manville Corporation which had operated the business as the Corrulux Division of Johns-Manville. (Admission 18, CX's 305C, M; Tr. 703.) [53]

118. In several of the years between 1963-1970 when Corrulux was owned by Johns-Manville, the business apparently had losses while in other years, there were small profits.[57] These losses or low profits, however, may have reflected the fact that as part of its intercorporate management policy, Johns-Manville allocated substantial general corporate expenses (for example, part of the cost of operating corporate jet aircraft) to the small Corrulux frp panel operation in Houston. (Tr. 708-09, 741, 743.)[58]

119. Johns-Manville had decided in 1970 either to close the Corrulux plant or to sell it. (RX 38; Tr. 790-91.)

120. In late 1971, Johns-Manville sold Corrulux to Simpson for notes and the assumption of liabilities. No cash was paid. Payment by Simpson consisted of a note for the full purchase price of $183,411. The plant and land were retained by Johns-Manville and leased to Simpson with an option to buy. (RX 47; Tr. 750.) [54]

121. After Simpson took over the Corrulux business, he attempted to eliminate inefficiencies which were traceable to the size, neglect, over-staffing, and extravagances of the Johns-Manville operation. (Tr. 709, 740-41, 748, 826.) Simpson described his business from the time he acquired Corrulux in December 1971 to the time he sold it in August 1974 as follows:

> We were carefully working our way toward a very substantial, profitable business . . . (Tr. 826.)
>
> . . . we demonstrated that [Corrulux] was a valuable, ongoing, viable business. (Tr. 827.)

122. The operation of Corrulux under Simpson was at least viable enough that a local bank in Houston and the Small Business Administration were persuaded to advance, renew, and guarantee

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[57] There is a difference between the parties as to whether Johns-Manville accurately reported earnings to Simpson prior to the sale. CX 74, which was given to Simpson by Johns-Manville, indicates profits in two of the three years between 1969-71. Respondent introduced RX's 38G and 46, Johns-Manville documents which seem to show losses in the time period 1963-1970. Neither side called a witness from Johns-Manville, and the exact condition of Corrulux prior to the Simpson acquisition remains an unresolved non-issue in this case.

[58] In addition, in 1971 Johns-Manville incurred extraordinary expenses in connection with the installation of certain machinery. (Tr. 707-08.) Simpson also testified that Johns-Manville neglected the business, and used it mainly as a training ground for plant managers. (Tr. 826.)

substantial loans to keep the business going. (CX's 12K, 14S; Tr. 721-23, 751-52, 816-17.)

123. The financial records of Corrulux show a profit of $58,374 for the fiscal year ending June 30, 1972, a loss of $35,761 for fiscal 1973, and a profit of $65,871 for fiscal 1974.[59] (CX's 11F, 12F, 14-o.) [55]

124. Although Corrulux produced frp panels in weights ranging from four to 12 ounces per square foot, most of its production was in the six to eight ounce industrial panel range. Almost all of Corrulux's production was of the heavier corrugated panels used in industrial applications such as skylights for pre-engineered metal buildings. Corrulux also produced some panels for the greenhouse application but little for use in the residential application. (CX's 53A-56D; Tr. 710-12, 784-85, 1723.)

125. There is no evidence in the record that the condition of Corrulux prior to the acquisition was such that bankruptcy was imminent.

126. There is no substantial evidence that the quality of Corrulux panels was below industry standards. The weight of the evidence is that Corrulux turned out commercially-acceptable panels which were regarded as [56] competitive in the industry. (CX's 18A, 311F, H; Tr. 356, 486, 565, 723-36, 972.)[60]

127. There is no evidence that Reichhold was the only available purchaser of Corrulux or that Corrulux made a serious effort to seek an alternative purchaser. Reichhold initiated the negotiations which resulted in the purchase of Corrulux in just two months. (Tr. 726-28.) No offer to sell Corrulux to any alternative purchaser was made by Simpson. (Tr. 486, 677, 731.) Simpson never advertised in any publication an offer to sell Corrulux; nor did Simpson ever contact a broker about selling Corrulux. (Tr. 732-33.) At least one other producer with a smaller market share than Reichhold, would have been "very interested" in at least examining the possibility of purchasing Corrulux had it been aware that Corrulux was for sale. (Tr. 974-75.)

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[59] According to respondent the fiscal 1974 profit was achieved entirely through an inventory write-up of $149,169 to reflect increase cost of resin. Reichhold argues that *its* corporate accounting practice was to reduce the value of its inventory (and its tax liability) by switching from FIFO (first-in, first-out) to LIFO (last-in, last-out) in 1974. Apparently, Internal Revenue Service allowed this change to be made to reflect the sharp increase in the value of inventories which resulted from the precipitous 1974 rise in the cost of resins produced from crude oil. Internal Revenue, however, indicated that later changes back to a LIFO system from FIFO might create serious tax consequences. (Tr. 1842-74.) Simpson considered making the accounting change and decided against it. (Tr. 811-12.) In any event, an independent certified accountant verified Corrulux's 1974 profit figure as consistent with accepted accounting procedure (Tr. 821) and it is not the function of an antitrust proceeding to weigh the tax and other considerations which may have motivated Reichhold to adopt one form of inventory costing while Corrulux decided to follow another.

[60] The former West Coast regional manager of Reichhold testified that prior to the acquisition "Corrulux was known to make a very good product . . . Corrulux made a very fine panel." (Tr. 972.) If Corrulux had some everyday quality problems this is not unusual: See Tr. 1526 for evidence of similar problems at Reichhold.

128. Reichhold acquired the Corrulux facilities in order to meet the sharp increase in demand for frp panels which appeared in late 1973 in the wake of the oil boycott and the fear by many frp panel buyers that there would be a permanent shortage of panels produced from oil-based resins. (Tr. 1876, 2039–40.)

129. This large demand for frp panels was almost immediately followed by the deep recession beginning in late 1974 which impacted severely on the frp panels business. (Tr. 580, 1729–30, 2035–36.) In the context of this drastic decline in frp sales, respondent reevaluated the entire Corrulux situation. This [57] reevaluation led to a conclusion by Reichhold management that the Corrulux operation produced an inferior product, that its equipment and building were in poor condition requiring a large capital outlay to correct, and that its product line was insufficiently automated to operate competitively. (RX 50; Tr. 2043–54, 2062.) This post-acquisition evaluation (at a time of deep recession) should be contrasted with a pre-acquisition report by a high Reichhold official that Corrulux's equipment "appeared well-kept and turned out commercially acceptable panels" (CX 18A; see also CX 6 and Tr. 805–06, 2043) and an independent pre-acquisition evaluation of Corrulux which concluded that the company was staffed with capable people (CX 311H) and that "The existing production line is a good piece of equipment, capable of producing competitive quality material at average line speeds in the order of magnitude of 25–30 ft. per minute." (CX 311F.)[61] [58]

130. The Corrulux plant was shut down by Reichhold in October 1975. (Answer ¶ 25.) At the present time Reichhold has not decided on whether to reopen the former Corrulux facility in Houston, Texas. (CX 313; Tr. 2057–58.)

131. As indicated in Finding 120, the building and land in Houston where Corrulux operated its business prior to the acquisition were not owned by Corrulux. Corrulux merely leased the building and land from Johns-Manville with an option to buy. One of

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[61] A high official of Reichhold even conceded that in one respect — catalyst injection — the Corrulux equipment was superior to Reichhold's and Reichhold modified its Grand Junction operation to conform to the Corrulux system. (Tr. 2072.) But another Reichhold officer testified that Corrulux's pre-acquisition expenditures for repairs, research, and quality control were "problems" and that its debt structure, compliance with safety and clear air regulations, collective bargaining agreement, dirty walls, uncut grass, age and inexperience of Mr. Simpson's son, Mr. Simpson's other business interests, and the unneat appearance of the storage areas troubled him. (Tr. 1827–42.) This evaluation may reflect in part a difference in standards between large, centrally controlled firms and small businesses. For example, when Simpson discovered that his resin tanks had jelled, he simply parked two milk trucks on the back lot and used these in place of the tanks. (Tr. 775, 821.) While a Reichhold official described this procedure as "remarkable" (Tr. 1838), he did not explain why it was not an acceptable innovation. Significantly, none of these "problems" described above were so overriding as to dissuade Reichhold from making the subject acquisition. (See Tr. 1964.) It should also be noted that a list of "problems" almost equally as long as the Corrulux list was drawn up by a Reichhold official for Reichhold's frp panel facility in Grand Junction, Tennessee. (RX 41E–1.)

the assets acquired by Reichhold from Corrulux was this option, and in 1975 Reichhold exercise the option by purchasing the building and land (8.3 acres) from Johns-Manville for about $300,000. (Admissions 23, 24, 25, CX's 305D, N; CX's 14F, 15A; Tr. 745, 1882–83.)

132. The Houston, Texas area is an especially attractive location for a potential frp panel producer because of its importance as a distribution center and its proximity to a large number of markets in which frp panels are used, especially the pre-engineered corrugated metal building market. (CX 17B; Tr. 1163, 2086–87.) [59]

III

DISCUSSION

This case involves a horizontal acquisition of a struggling company doing business in a relatively small industry. But neither the less than robust condition of Corrulux nor the size of the frp panel industry can somehow combine to immunize this acquisition from the reach of Section 7. *United States* v. *Third Nat. Bank,* 390 U.S. 171 (1968); *FTC* v. *Food Town Stores, Inc.,* 539 F.2d 1339 (4th Cir. 1976). Instead, this case must turn on resolution of the usual legal and factual issues which arise when one competitor acquires another.

On the threshold question of market definition, it is important that the frp panel producers themselves act as if the production of frp panels is a market. By this I mean that the frp panel producers, (a readily identifiable cluster of suppliers) conceive of competition as vying against each other to serve a perceived preference for frp panels. The panel producers testified with almost complete unanimity that they were only concerned about the prices charged by other frp panel producers, that they only compete against other frp panel producers, that they do not compete against producers of other materials, and that they do not react competitively to the prices charged by producers of these other materials.[62] Such supply-side perceptions are important because a significant reduction in the number of frp panel producers and the creation of a more concentrated market structure may lead in turn to a hightened potential for oligopolistic pricing among the survivors who commonly share this insulated view of competition. *United States* v. *Philadelphia Nat. Bank,* 374 U.S. 321 (1963). Thus, it is of small comfort to frp users to suggest that aluminum, glass, or polyethylene film may be substitutes for frp panels in some appli[60]cations when the record plainly shows (1) that frp panel producers set their prices without reference to what manufacturers of other materials may do, and (2) in actual practice, the prices charged for frp panels show little or no sensitivity to the prices charged for other materials.[63]

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[62] Findings 32, 43, 53, 75, 77–79.

This supply-side view of competition as well as the price insensitivity derives initially from the existence of a demand for frp panels for use in such applications as industrial skylights and sidelights, liners, patios, and greenhouse covers. In some of these applications (patios and greenhouses) clearly other materials can be used and are being used, but frp panels are preferred by a not insignificant number of buyers.[64] In other applications (corrugated building skylights and sidelights and refrigerated car liners), the preference is so marked that frp panels have for all practical purposes become the standard, non-substitutable material.[65] In all of their applications, the preferences for frp panels are based on either physical characteristics or cost considerations or both.

Although the preference for frp panels varies in intensity depending upon the use to which the product is being put, the frp panel producers, as I indicated above, essentially conceive of themselves as competing to sell to customers located somewhere within this spectrum of preferences. This view of competition, shared by all major frp producers, is fortified by other circumstances. [61]

First, the supply-side view of competition is influenced by the fact that most firms in the industry share a common production technique which is not used to produce any other product. In addition, the frp manufacturers all face roughly similar raw material costs, and even when there are certain exceptions to this pattern, as in the cases of vertically integrated Reichhold and Filon, the exceptions are recognized by non-integrated producers as competitive advantages within the frp panel industry itself.[66]

Second, the frp panel producers are either companies which make only frp panels, or as divisions of multi-product corporations they function as separate entities whose main products are frp panels. This means that organizationally frp panel producers operate in such a way that their efforts are directed solely to the market for frp panels.[67]

Third, because the main frp producers are confronted with common technical and marketing problems they find themselves joined together in a single trade group formed to solve these problems. This further tends to identify and limit their perceptions of competition.[68]

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[63] Findings 31 (note 20), 32, 33, 43, 53, 64, 74, 75, 77–80.

[64] Findings 28–31, 34, 66–74.

[65] Findings 35–54.

[66] Findings 17–21, 97.

[67] Finding 81.

Following *Brown Shoe*,[69] similar considerations — industry or public recognition of a separate economic entity, peculiar characteristics and uses, unique production facilities, distinct customers, distinct prices, sensitivity to price changes, and specialized [62] vendors — have been used to delineate submarkets within broader product markets which include products that may be substitutable.

It is well-settled that not all the *Brown Shoe* criteria must be met before a relevant product submarket is found.[70] See, *General Foods Corporation* v. *FTC*, 386 F.2d 936 (3rd Cir. 1967), *cert. denied*, 391 U.S. 919 (1968); *Reynolds Metals Company* v. *FTC*, 309 F.2d 223 (D.C. Cir. 1962). The courts and the Commission have only required the existence of practical indicia of an area of effective competition. See, *e.g., United States* v. *Aluminum Co. of America (Rome Cable)*, 377 U.S. 271 (1964) (Aluminum conductor was held to be a submarket despite the existence of copper competition. The Supreme Court said that user preference for aluminum in certain conductor applications and the lack of price sensitivity between the two materials were enough to establish a separate market.); *Beatrice Foods Co.* v. *FTC*, 540 F.2d 303 (7th Cir. 1976) (Paint brushes and rollers were held to be a separate line of commerce distinct from aerosols and sprayers even though all were interchangeable for some applications. A separate market was defined on the basis of different manufacturing processes and raw material costs, distinct prices, and the fact that brush and roller manufacturers did not take into account the prices of aerosols and sprayers.); *Avnet, Inc.* v. *FTC*, 511 F.2d 70 (7th Cir. 1975), *cert. denied*, 423 U.S. 833 (1975) (New automotive electrical units held to be a separate market from reconditioned units since there was an absence of any substantial interaction in price between the two lines.); *Reynolds Metals Company* v. *FTC*, 309 F.2d 223 (D.C. Cir. 1962) (Florist foil constitutes a relevant market although it was largely indistinguishable from other types of decorative aluminum foil, but buyer preference had [63] established distinct prices.); *United States* v. *Mrs. Smith's Pie Company*, No. 74-419, slip op. (E.D. Pa. November 18, 1976) (Frozen pies constitute a separate submarket although they are interchangeable with many other desserts and there is a degree of price sensitivity among all desserts. Separate market found on basis of unique production facilities, unique distribution channels, preferences of some consumers, and perceptions of frozen pie producers as to their competition.); *United States* v. *American Technical Industries, Inc.*, 1974-1 Trade Cases ¶ 74,873 (M.D. Pa. 1974) (Artificial Christmas trees constitute a separate line of commerce even though interchangeable with natural Christmas trees in the sense that both products are sold to the same class of ultimate consumer for the same end use. Separate market finding based on the existence of a separate group of manufacturers for each kind of tree, differences in production facilities and prices, as well as general recognition of an artificial tree submarket.); *United States* v. *Pennzoil Company*, 252 F. Supp. 962 (W.D. Pa. 1965) (Penn Grade oil was found to be a relevant submarket although other oils served the same end use as lubricants. Separate submarket based on physical characteristics — Penn Grade has a paraffin base and is freer of impurities — as well as existence of separate trade association, distinct customers, and price differences.); *United States* v. *Aluminum Company of America (Cupples)*, 233 F. Supp. 718 (E.D. Mo. 1964), *aff'd per curiam*, 382 U.S. 12 (1965) (Aluminum curtain wall held to be distinct from precast concrete and stainless steel curtain walls on basis of separate trade association, distinct physical characteristics — *i.e.*, colors and pliability — and distinct prices.); *Union Carbide Corp.*, 59 F.T.C. 614 (1961) (The existence of adequate substitute packaging material does not erase the fact that buyers who prefer polyethylene film constitute a separate market.).

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[68] Findings 82-87.

[69] *Brown Shoe Co.* v. *United States*, 370 U.S. 294 (1962).

[70] Here, for example, in the patio and greenhouse applications there are no specialized vendors of frp panels. See Finding 88.

These precedents tend to support the conclusion that even in the greenhouse and patio applications frp panels constitute a relevant submarket although other [64] materials may serve the same general purpose. The trade realities are that irrespective of the existence of possible substitutes, the frp producers compete to serve the perceived preference for frp panels among consumers who, for example, desire muted light rather than shade for their patios, or cut flower growers who select frp panels over glass or polyethylene film for reason of diffused light transmission, durability, and cost.[71] Moreover, for at least two important applications of frp panels — the corrugated metal building and refrigerated van liner uses — there is no evidence whatever of any practical substitutes.[72]

On the basis of all the factors outlined above, I have concluded that the manufacture of frp panels is a submarket for Section 7 analysis. I reach this conclusion from the record evidence relating to the preference of buyers based upon physical characteristics and costs, as well as the proof relating to how frp panel producers perceive the competitive significance of these preferences. These preferences on the demand side and perceptions on the supply side combine to form as "area of effective competition."[73] Within this area of effective competition, any significant reduction in the [65] number of frp producers may have anticompetitive consequences irrespective of what the aluminum, glass, polyethylene film, acrylic or other manufacturers may do.

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[71] While the record indicates that frp panels fulfill a unique range of applications (see Findings 23), complaint counsel failed to prove that this range, taken alone, has any special economic significance on either the supply or demand sides. In addition, with respect to use of frp panels in several specific applications — garage doors, glazing, water towers, and signs — complaint counsel failed to offer adequate proof that these uses constitute proof of a relevant frp submarket. (Findings 55-59.)

[72] Findings 42, 49.

That this frp panel market is small in over-all size is not a material consideration for Section 7 purposes. Buyers of frp panels, like customers of major industrial products, are fully entitled to be protected from the potential anticompetitive effects of concentration and the elimination of actual competition. *United States* v. *Phillipsburg Nat. Bank,* 399 U.S. 350 (1970); *Ekco Products Co.,* 65 F.T.C. 1163 (1964), *aff'd,* 347 F.2d 745 (7th Cir. 1965); *Reynolds Metals Co.,* 56 F.T.C. 743 (1960), *aff'd,* 309 F.2d 223 (D.C. Cir. 1962).

Even before the acquisition, the frp panel market was highly concentrated with four firms, including Reichhold, controlling 68 percent of production.[74] Prior to the acquisition, Reichhold ranked second with 18.85 percent of the market and Corrulux ranked seventh with 4.45 percent.[75] The 1974 Corrulux acquisition raised Reichhold to first in market share with 23.3 percent and increased the level of four firm concentration from 68.83 percent to 73.28 percent.[76] Eight firm concentration rose from 89.26 percent to 92.85 percent.[77]

Considering the concentrated state of this industry, even a small increase in concentration may have been suspect. The Corrulux acquisition, however, was not *de minimis* by any standard. Horizontal acquisitions involving much smaller market shares have been proscribed [66] under Section 7, *Stanley Works* v. *FTC,* 469 F.2d 498 (2nd Cir. 1972), and, in general, the well-established precedents simply do not permit the second ranking company to eliminate the seventh ranking firm in concentrated industries. *United States* v. *Pabst Brewing Co.,* 384 U.S. 546 (1966); *United States* v. *Von's Grocery Co.,* 384 U.S. 270 (1966); *Aluminum Company of America* v. *United States,* 377 U.S. 271 (1964); *United States* v. *Philadelphia Nat. Bank,* 374 U.S. 321 (1963).

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[73] *United States* v. *du Pont & Co. (General Motors),* 353 U.S. 586, 593 (1957), quoting from, *Standard Oil Co. of California* v. *United States,* 337 U.S. 293, 299, n. 5 (1949).

[74] Finding 104.

[75] Finding 103.

[76] Findings 103, 104.

[77] Finding 104.

Given the existing state of concentration and the increase in concentration resulting from the Corrulux acquisition, it is irrelevant that the industry may have retained some characteristics which could conceivably lead to price competition. Respondent thus seeks to attach undue importance to whatever over-capacity exists in the industry, and the argument that this condition may constitute a countervailing influence which diminishes the effects of concentration is not persuasive for several reasons. In the first place, the rate of plant utilization fluctuates to the point where it can hardly excuse a permanent structural change brought about by a horizontal acquisition. For example, from mid-1973 to early 1974 the over-capacity condition largely evaporated, and this appears to be happening again in 1977.[78] Also, the seasonal nature of frp production tends to distort the industry's annualized utilization rate.[79] Moreover, there is no proof in the record of actual excess production, and there is evidence that over-capacity is not so costly to maintain that it acts as a constant spur to price competition.[80]

Assuming, however, that the historical pattern in the industry has been one of chronic over-capacity and that over-capacity has inspired some price competition, [67] it is somewhat incongruous for respondent to argue that this condition can justify an acquisition which gives the second ranking company the power to reduce that very over-capacity by summarily shutting down the acquired plant of the seventh ranking company. Respondent has not yet satisfactorily explained how, on the one hand, it can say that over-capacity tends to keep the industry competitive, while, on the other hand, it seeks to justify an acquisition which resulted in an almost immediate reduction in industry capacity when Reichhold decided to close down the Corrulux plant after the acquisition.[81] Besides, even if over-capacity is endemic to the frp panel industry, by concentrating production in fewer hands respondent has created a market structure which is more conducive to an industry-wide agreement, tactic or otherwise, which may attempt to solve this "problem" by fixing prices or limiting production.[82]

As to respondent's arguments about present-day low profits and the vigor of competition in the industry, even if the facts were so[83] these conditions would hardly justify a substantial horizontal acquisition. Section 7 was intended to arrest anticompetitive tendencies in their incipiency: the Congressional assumptions being that competition is best served by having competitively structural markets and, conversely, that as markets gravitate toward domination by a few firms the potential for adverse consequences grows. Considering the basic purpose of Section 7 — to stop the trend toward potentially anticompetitive market structures — the acquisition of one competitor by [68] another and the creation or perpetuation of a tendency toward a concentrated market cannot be excused on the grounds that some indicia of competition still remain or that the industry is competitive enough. *United States* v. *Von's Grocery Co.*, 384 U.S. 270 (1965); *Brown Shoe Co.* v. *United States,* 370 U.S. 294 (1962).

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[78] Finding 113.

[79] Finding 113.

[80] Finding 114.

[81] Finding 130.

[82] Bain, INDUSTRIAL ORGANIZATION 170 (1959).

[83] See Findings 110-115.

Respondent's reliance on *United States* v. *Crowell, Collier and Macmillan Inc.*, 361 F. Supp. 983 (S.D.N.Y. 1973) as suggesting a contrary rule, namely, that low profits may indicate no adverse effect from concentration is misplaced. For even in *Crowell, Collier,* in which a district court said that an acquiring company with a 41.9 percent market share had little ability to affect competition and that a market in which the top four firms accounted for 69.6 percent showed "no indication of a trend toward concentration" (*Id.* at 994), the court did *not* say that a significant increase in concentration and the resulting potentiality for anticompetitive effects are to be weighed against a past history of low profit margins or unused capacity. *Crowell, Collier* rests on *de minimis* analysis: the acquired company accounted for less than 1 percent of the relevant market, and the court intimates the likelihood of an entirely different result were the acquired firm's market share as much as the 1.3 percent involved in *Stanley Works.*

As for the existence or non-existence of entry barriers, this too is also largely beside the point in a market in which concentration is already great and a high-ranking actual competitor is eliminated. The Commission has plainly held that the elimination of an actual competitor is *not* to be balanced against the possibility that because entry barriers may be low, a new entrant may sometime appear. *Ekco Products Co.*, 65 F.T.C. 1163 (1964), *aff'd,* 347 F.2d 745 (7th [69] Cir. 1965).[84] As it happens, while the capital outlay required to enter the frp panel market is not large, a potential entrant may be deterred from trying to wrest away a more than insignificant market share in an industry where Reichhold and Filon control close to 45 percent of the market and both of these large companies enjoy the obvious advantage of having an assured and integrated supply of the raw material.[85] The track record of the industry has been that with one exception, Kalwall, there have been no entrants *de novo* in the past 10 years or more.[86] On the other hand, there is indication of a trend toward acquisitions of frp panel producers by large firms, including three such acquisitions by respondent Reichhold.[87] [70]

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[84] In *Ekco,* the Commission said:

> Ease of entry may, to be sure, cause the market power of established firms to be eroded by the advent of significant new competitors; but this is likely to be at best a long-term affair. See Bok, *Section 7 of the Clayton Act and the Merging of Law and Economics,* 74 Harv. L. Rev. 226, 260 (1960). Ease of entry may also induce the firms active in the relevant market to keep their prices down to an entry-discouraging level; but that does not mean that such an entry-discouraging price level if likely to be as low as the level that would prevail if there were actual competition in the market. . . In short, the absence of high entry barriers cannot be depended upon to ensure effectively competitive conditions. *Cf.* Bain, Barriers To New Competition 189 (1956); Bain Industrial Organization 425 (1959). 65 F.T.C. 1163, 1208.

Respondent also argues that because Corrulux at the time of the acquisition was a high cost, low profit producer, and had not been able to penetrate the residential market, this somehow brings this acquisition within the *General Dynamics*[88] decision. Not only does this argument totally ignore the record facts — Corrulux was the seventh ranking firm, made a small profit before the acquisition, and, in general, was a struggling but viable company which was making progress[89] — but more important, it is inadequate as a matter of law. Complaint counsel had no burden to prove that the acquired company was an aggressive price cutter whose acquisition eliminated actual price competition. Again, it must be noted that Section 7 is an incipiency statute aimed at preventing the creation or perpetuation of concentrated market structures which *may* lead potentially to anticompetitive effects. *United States* v. *Von's Grocery Co.,* 384 U.S. 270 (1966). No proof of *actual* anticompetitive effects on price has been required in any case including *General Dynamics.*[90] Nor can *General Dynamics Corp.* be read as saying that evidence of high concentration ratios in a relevant market must be balanced against the "problems" facing the acquired company, or that these everyday problems of a business somehow excuse its elimination. In *General Dynamics,* The Supreme Court was looking to deep-rooted and permanent changes (in that case, the ability of the acquired company to compete for long-term requirement contracts in the face of depletion of its coal reserves) which impacted on the quantitative significance of the acquisition. There is nothing, however, in *General Dynamics* which says that fluctuations in prices, costs, or profits are to be weighed routinely in Section 7 cases as countervailing factors which may diminish the effects [71] of a permanent structural change brought about by the acquisition. *United States* v. *Amax, Inc.*, 402 F. Supp. 956, 970–71 (D. Conn. 1975).

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[85] Finding 97.

[86] Finding 99.

[87] Findings 100-101.

[88] *United States* v. *General Dynamics Corp.,* 415 U.S. 486 (1974).

[89] Findings 91, 116-126, 129.

[90] 415 U.S. at 505.

General Dynamics also confirms the rule, earlier stated by the Commission in *Procter & Gamble Co.*,[91] that postacquisition evidence is of "extremely limited" probative value for the obvious reason that divestiture under Section 7 could be avoided "merely by refraining from aggressive or anticompetitive behavior when such a suit was threatened or pending." 415 U.S. 486, 504–05. Consistent with this precedent, it is of no moment that Reichhold's market share may have declined in the period 1974 to 1976 from the 23 percent which resulted from the acquisition. (See Respondent's Reply Brief, p. 29.) This decline may be attributable to any number of temporary influences (including the special vulnerability of the Reichhold line to the severe 1974–75 recession), as well as internal business decisions which could be reversed once this litigation is over, say, a decision to reopen the Corrulux plant.

As for the condition of Corrulux, respondent seems to be saying not only that Corrulux was weak at the time of the acquisition in August 1974, but also that it "failed" permanently in October 1975 when Reichhold closed the former Corrulux plant. If this argument is intended (as respondent's answer to the complaint intimates) as a strained version of the strict requirements of the failing company defense as stated in *International Shoe Co.* v. *FTC*, 280 U.S. 291 (1930) and *Citizen Publishing Co.* v. *United States*, 394 U.S. 131 (1969),[92] it misses the mark by a wide margin. [72]

The record indicates that notwithstanding its low profits, Corrulux was a viable company prior to the acquisition. According to Reichhold, however, *after* the acquisition, the corporate officials of Reichhold made an assessment of Corrulux and decided that Corrulux did not meet Reichhold's standards of quality and efficiency; therefore, they decided to close the plant, and thus Corrulux "failed" in a fashion. As respondent would have it, there is a defense to a Section 7 charge which allows a major corporation to acquire a smaller competitor, evaluate that competitor in terms of *Reichhold's* criteria and then discard the acquired company as a

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[91] 63 F.T.C. 1465 (1963), *aff'd*, 386 U.S. 568 (1967).

[92] The usual statement of the "failing company" defense is that (1) the prospects of reorganization under Chapter X or Chapter XI of the Bankruptcy Act were dim or nonexistent and (2) there was no other, less anticompetitive sale feasible. *Citizen Publishing Co.* v. *United States*, 394 U.S. 131 (1969). The "failing company" defense is not easily made. There must, for example, be a showing of unsuccessful attempts to get financing, evidence of deep concern by creditors, a generally tenuous and debilitated financial situation, threats of withdrawal of lines of credit, check "kitting," and failure to pay bills. As for the second leg of the defense — no other feasible buyer available — the proponent of the defense must show a deliberate attempt to locate a prospective purchaser by contacting brokers and other means. *United States* v. *M.P.M. Inc.*, 397 F. Supp. 78 (D.C. Colo. 1975). Respondent herein met *none* of the requirements of the "failing company" defense. See Findings 116–127.

"failure," in the sense that it fails to come up to *Reichhold's* intracorporate standards for profitability and efficiency.

There is no such quasi-failing company defense available under Section 7 of the Clayton Act. The market is supposed to determine whether firms fail or not, and the very purpose of the "failing company" doctrine is to preserve (and not discard as Reichhold did) an entity which would have collapsed but for the acquisition. *International Shoe Co.* v. *FTC*, 280 U.S. 291 (1930). As for the use by a large firm of *its* [73] internal standards to determine whether a small competitor fails or not, the legislative history of Section 7 indicates that the Congressional intent was just the opposite — Congress wanted to stop acquisitions which give large firms discretionary power over the continued development or, for that matter, the existence of their smaller competitors. *Crown Zellerbach Corp.* v. *FTC*, 296 F.2d 800 (9th Cir. 1961), *cert. denied*, 370 U.S. 937; see also concurring opinion of Mr. Justice Douglas in *United States* v. *Falstaff Brewing Corp.*, 410 U.S. 526, 538 (1973).

In sum, this acquisition is patently illegal and indefensible, and respondent must bend every effort to restore Corrulux as a viable, independent competitor. *Ford Motor Co.* v. *United States*, 405 U.S. 562 (1972); *Ekco Products Co.*, 65 F.T.C. 1163, 1212-17 (1964), *aff'd*, 347 F.2d 745 (7th Cir. 1965). It is especially important that divestiture should be required of *all* of the property which Reichhold acquired as a result of the acquisition including the plant and land which were obtained when Reichhold exercised the option originally owned by Corrulux.[93] The record indicates that Houston is a particularly attractive location for an frp panel plant, and the prospect of obtaining a desirable Houston location may constitute the best hope for attracting a new entrant.[94] Certainly Reichhold should not be allowed to delay or manipulate the sale of the former Corrulux assets (which included the option to buy the plant and land) in such a way that profit from the possible appreciation in the value of the real estate becomes a material consideration in the divestiture process to the point where prospective entrants are discouraged. Reichhold has no right to [74] profit from this unlawful acquisition, *United States* v. *Papercraft Corporation*, 393 F. Supp. 415 (W.D. Pa. 1975), *rev'd on other grounds*, 540 F.2d 131 (1976), and any insistence on a profit from the sale of plant and land, which may indeed have appreciated in value, may only result in establishing such a high value for Corrulux that no prospective buyer will emerge. The order which I will issue, therefore, will require that respondent divest itself absolutely within one year of all the assets which it acquired as a result of the Corrulux acquisition including the plant and real estate. Furthermore, given the high level of concentration in the frp panel industry, the small number of independent firms which remain, and Reichhold's proven proclivity to acquire frp panel manufacturers,[95] a ten year ban on future acquisitions unless the Commission gives its approval is fully warranted. *Ekco Products Co.,* 65 F.T.C. 1163 (1964).

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[93] Finding 131.

[94] Finding 132.

In addition, the order will require that any improvements in the Corrulux equipment which were made subsequent to the acquisition be divested. The record shows, for example, that Reichhold installed new machinery for cutting panels at the Corrulux plant and then removed this equipment when the plant was closed. (Tr. 2055-56.)[96] This new cutting equipment was an improvement dictated by the decibel requirements of OSHA. (Tr. 2051-52.) This equipment should be restored to the Corrulux plant for inclusion in the divested assets. An industry does not remain frozen during the period of unlawful retention of the acquired company and divestiture of an outmoded firm with no [75] chance of survival makes neither technological nor competitive sense. The Commission may properly order that the acquired firm be recreated in such form as would reflect the firm's probable growth, including improvements it may have added itself. *Union Carbide Corp.,* 59 F.T.C. 646 (1961); Elzinga, *The Antimerger Law: Pyrrhic Victories,* 12 Journal of L. & Econ. 43 (1969).

To further the goal of creating at least a reasonable opportunity for a restored Corrulux to succeed, the order also will contain provisions for (1) an assured source of supply of resin from Reichhold at the best market price and a requirement that Reichhold provide the acquirer with know-how; (2) a two-year prohibition against a solicitation by Reichhold of former Corrulux customers; and (3) a requirement that respondent make available to the new owners Reichhold's frp panel customer list. These provisions are all designed, in the language of *Ford Motor Co.,* ". . .to give the divested plant an opportunity to establish its competitive position" and the time it needs to "obtain a foothold in the industry."[97]

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[95] Finding 100.

[96] Still other improvements have not been removed. (Tr. 2051-52.) The order is intended to cover *all* improvements, whether removed or not.

[97] 405 U.S. at 575.

IV

CONCLUSIONS OF LAW

1. The Federal Trade Commission has jurisdiction over the subject matter of this proceeding and over respondent Reichhold.

2. On or about August 19, 1974, Reichhold acquired all of the assets of Corrulux.

3. At all times relevant to this proceeding, Reichhold and Corrulux were engaged in commerce within the meaning of the Clayton Act and the Federal Trade Commission Act. [76]

4. For the purpose of assessing the legality of the acquisition under Section 7 of the Clayton Act, the appropriate line of commerce is the manufacture and distribution of frp panels.

5. The United States as a whole is an appropriate section of the country within which to test the effects of the acquisition.

6. Prior to and at the time of the acquisition, Reichhold and Corrulux were actual competitors in the United States frp panel market.

7. The acquisition eliminated substantial actual competition between Reichhold and Corrulux in the frp panel market.

8. The acquisition substantially increased concentration in the frp panel market.

9. The effect of the acquisition of Corrulux by Reichhold may be substantially to lessen competition in the frp panel market in the United States, in violation of Section 7 of the Clayton Act and Section 5 of the Federal Trade Commission Act.

10. Divestiture including all improvements and all after-acquired property is both necessary and appropriate to remedy the anticompetitive effects of this unlawful acquisition. In addition, Reichhold should be required to supply resin to the divested Corrulux for three years and to forbear from contacting former Corrulux customers for two years. Reichhold should also be prohibited from acquiring any frp panel producer, without prior approval of the Federal Trade Commission, for a period of 10 years.

Accordingly, the following order will be issued: [77]

ORDER

I

It is ordered, That respondent, Reichhold Chemicals, Inc. (hereinafter "Reichhold"), a corporation, and its officers, directors, agents, representatives, employees, subsidiaries, affiliates, successors and assigns, shall divest all assets, title, properties, interest, rights and privileges, of whatever nature, tangible and intangible, including without limitation all real property, buildings, machinery, equipment, raw material reserves, inventory, customer lists, trade names, trademarks, and other property of whatever description acquired by Reichhold as a result of its acquisition of The Corrulux Corporation (hereinafter "Corrulux") together with all additions and improvements to Corrulux which have been made subsequent to the acquisition. Such divestiture shall be absolute, shall be accomplished no later than one (1) year from the service of this order, and shall be subject to the prior approval of the Federal Trade Commission. [78]

II

It is further ordered, That pursuant to the requirements of Paragraph I, none of the stock, assets, properties, rights, privileges and interests of whatever nature, tangible or intangible, acquired or added by Reichhold, shall be divested, directly or indirectly, to anyone who is at the time of the divestiture an officer, director, employee or agent of, or under the control, direction or influence of Reichhold, or anyone who owns or controls, directly or indirectly more than one (1) percent of the outstanding shares of the capital stock of Reichhold or to anyone who is not approved in advance by the Federal Trade Commission.

III

It is further ordered, That pending the divestiture required by this order, respondent shall not knowingly cause or permit the deterioration of the assets and properties specified in Paragraph I in a manner that impairs the marketability of any such assets and properties. [79]

IV

It is further ordered, That at the time of the divestiture required by this order, respondent shall make available to the acquirer of the divested assets a list of all of respondent's customers for fiberglass reinforced panels who have purchased said panels from respondent within three years prior to the date this order becomes final.

V

It is further ordered, That respondent, for a period of two (2) years from the date this order becomes final, shall not solicit (for the purpose of selling fiberglass reinforced plastic panels) any customer who purchased said panels from Corrulux during the year prior to the acquisition by respondent of Corrulux.

VI

It is further ordered, That for a period of one (1) year following the divestiture required by this order, respondent shall provide the acquirer of the divested assets, if the acquirer so requests, such know-how as [80] may reasonably be required to enable such acquirer to manufacture and sell fiberglass reinforced plastic panels. For a period of three (3) years following the divestiture required by this order, respondent shall provide the acquirer of the divested assets, if the acquirer so requests, such amounts of suitable polyester resin as the acquirer may reasonably need to produce fiberglass reinforced plastic panels. Respondent shall charge the acquirer no more than its own costs for providing know-how. Respondent shall charge the acquirer no more than the lowest price that it is then charging, on the open market, regardless of volume, for polyester resin.

VII

It is further ordered, That, for a period commencing on the effective date of this order and continuing for ten (10) years from and after the date of completing the divestiture required by this order, Reichhold shall cease and desist from acquiring, directly or indirectly, without the prior approval of the Federal Trade Commission, the whole or any part of the stock, share [81] capital, assets, any interest in or any interest of, any domestic concern, corporate or noncorporate, engaged in the manufacture, production, distribution or sale of frp panels nor shall Reichhold enter into any arrangement with any such concern by which Reichhold obtains the market share, in whole or in part, of such concern.

VIII

It is further ordered, That on the first anniversary date of the effective date of this order and on each anniversary date thereafter until the expiration of the prohibitions in Paragraph VII of this order, Reichhold shall submit a report in writing to the Federal Trade Commission listing all acquisitions, mergers and agreements to acquire or merge made by Reichhold; the date of each such acquisition, merger or agreement; the products involved and such additional information as may from time to time be required.

IX

It is further ordered, That within thirty (30) days from the effective date of this order and every sixty (60) days thereafter, until it has fully complied with [82] Paragraph I of this order, Reichhold shall submit a verified report in writing to the Federal Trade Commission setting forth in detail the manner and form in which it intends to comply, is complying or has complied therewith. All such reports shall include, in addition to such other information and documentation as may hereafter be requested, (a) a specification of the steps taken by Reichhold to make public its desire to divest Corrulux, (b) a list of all persons or organizations to whom notice of divestiture has been given, (c) a summary of all discussions and negotiations together with the identity and address of all interested persons or organizations, and (d) copies of all reports, internal memoranda, offers, counteroffers, communications and correspondence concerning said divestiture.

X

It is further ordered, That respondent shall notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent such as dissolution, assignment or sale resulting in the [83] emergence of a successor corporation, or any other proposed change in the corporation, which may affect compliance obligations arising out of this order.

FINAL ORDER

This matter having been heard by the Commission upon the appeal of respondent from the initial decision; and

The Commission having considered the oral arguments of counsel, their briefs, and the whole record; and

The Commission having denied in full the appeal of respondent's counsel; and

The Commission having determined that the initial decision and order contained therein shall become the decision and order of the Commission, with the following changes:

Page 15, substitute for Finding 21:

21. Except for the limited number of instances noted earlier which amount to no more than about 7 percent of industry frp panel production (Findings 19, 20), all of the producers of frp panels use the continuous line process (CX's 306A, B; RX 83, pp. 9-10; Tr. 311, 313-14, 928, 1180). [2]

Page 46, footnote 53, line 21, change "competition" to "conversion."

Page 52, Finding 115, add at end of line:

> The rates of return on equity in 1974 for frp panel producers Fiberglass Plastics, Inc. and Kemlite Corporation were 35 percent and 28 percent respectively (CX's 189B, C, 122R). Kemlite's average annual rate of return on equity for 1965-74 was 23 percent (CX 122R).

Page 64, substitute for footnote 71:

> [71] The record indicates that frp panels fulfill a unique range of applications (See Finding 23). While such versatility may constitute a "peculiar characteristic" under *Brown Shoe,* or otherwise contribute to the finding of a relevant submarket, see, *e.g., General Foods Corp.,* 69 F.T.C. 380, 415 (1966), *aff'd,* 386 F.2d 936 (2d Cir. 1967), *cert. denied,* 391 U.S. 919 (1968); *Brillo Mfg. Co., Inc.,* 64 F.T.C. 245, 253-54 (1963); *Union Carbide Corp.,* 59 F.T.C. 614, 654 (1961), we are not persuaded of its relevance here. The record does not show, for example, that this versatility is a basis for consumer preference or that it enables producers to withstand fluctuations in demand for particular end uses better than producers of substitute products which are less versatile.
>
> In addition, complaint counsel failed to demonstrate the significance to an frp submarket of the use of frp panels in garage doors, glazing, water towers, and signs (Findings 55-59).

Page 72, footnote 92, line 7, change "kitting" to "kiting."

Page 75, delete lines 5-8 beginning with "*Union Carbide*" and substitute:

> *United States* v. *Aluminum Co. of America,* 247 F. Supp. 308, 316 (E.D. Mo. 1964), *aff'd mem.,* 382 U.S. 12 (1965) (order required divestiture of plant built after unlawful acquisition); *Union Carbide Corp., supra,* 59 F.T.C. at 657, 673 (divestiture of all post-acquisition improvements and equipment installed on premises of acquired company); see generally Elzinga, *The Antimerger Law: Pyrrhic Victories,* 12 Journal of L. & Econ. 43 (1969). [3]

Page 75, line 13, following "best market price" add "[97]," with text of footnote as follows:

> [97] See *United States* v. *Kennecott Copper Corp.,* 249 F. supp. 154, 162 (S.D.N.Y.), *aff'd mem.,* 381 U.S. 414 (1965); cf. *Ford Motor Co.* v. *United States, supra,* 405 U.S. at 572.

Page 75, line 22, change "[97]" to "[98]," and renumber footnote accordingly.

Therefore, it is ordered, That the initial decision (as modified

above) and the order contained therein, shall become the decision and order of the Commission on the date of issuance of this order.

IN THE MATTER OF

POWER'S SERVICE, INC., ET AL.

Docket C-2810. Interlocutory Order, Feb. 22, 1978

Denial of motion to reopen proceeding and modify order to cease and desist on grounds that such motion was premature given the Commission has still before it a similar case involving related issues.

ORDER DENYING PETITION TO REOPEN PROCEEDING AND MODIFY ORDER TO CEASE AND DESIST

By letter filed on October 18, 1977, petitioners, who prepare and send debt collection forms on behalf of creditors, have requested the Commission to modify the consent order issued in the above-captioned matter on March 11, 1976. The modification sought is the deletion of the disclosure required by Paragraph 4 of the order. Petitioners' letter with supporting documents is being treated as a petition to reopen the proceeding and modify the order under Rule 3.72(b)(2) of the Commission's Rules of Practice. The Bureau of Consumer Protection opposes modification of the order as premature.

Paragraph 4 requires petitioners to disclose in each communication sent to alleged delinquent debtors the following statement: "This communication is only a reminder notice. Power's Service, Inc. cannot accept payment nor will it take legal action regarding this claim." Paragraph 4 also sets certain standards for the size and color of this required disclosure.

Petitioners' request for modification is based on their assertion that the disclosure required by paragraph 4 places them at a competitive disadvantage with various competitors who are not under any cease and desist order requiring such disclosure. Furthermore, petitioners allege that ever since they began to place the required disclosure in their debt collection communications, they have suffered a decline in sales, which they state is due to the use of the disclosure. Petitioners also cite the following two decisions rendered by Administrative Law Judges in two Commission proceedings in which order provisions similar to the one they wish modified have been rejected. *In the Matter of Trans World Accounts, Inc., et al.,* Dkt. 9059 (1977), and *In the Matter of Capax, Inc., et al.,* Dkt. 9058 (1977).

Rule 3.72(b) of the Commission's Rules of Practice provides for modification of an order upon a showing by petitioners that changed conditions of fact or law require such modification or that the public interest so requires.

The Commission has issued a final order in *Trans World Accounts* [90 F.T.C. 350]. Complaint counsel did not appeal from the Administrative Law Judge's determination to reject a provision requiring an affirmative disclosure in respondents' collection notices. The Commission, therefore, did not consider its propriety in that case.

The appeal in *Capax* is currently pending before the Commission. Since it involves issues related to those raised by the instant petition, the Commission has determined that the petition is premature:

Accordingly, the Commission having carefully considered the petition and the answer thereto and being of the opinion that the petition is untimely:

It is ordered, That petitioners' petition be, and it hereby is, denied without prejudice.

IN THE MATTER OF

DAMON CORPORATION

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT AND SEC. 7 OF THE CLAYTON ACT

Docket C-2916. Complaint, Feb. 23, 1978 — Decision, Feb. 23, 1978

This consent order, among other things, bars a Needham Heights, Mass. operator of a chain of medical laboratories from acquiring, for a period of ten years, any independent medical laboratory located in, or doing 25% or more of its business in given markets, without prior Commission approval. Further, the order requires the firm to cease furnishing any means of compensation to physicians or others for referring specimens for testing to Damon laboratories, rather than to those of its competitors.

Appearances

For the Commission: *Andrew G. Stone* and *Randolph B. Sim.*

For the respondent: *Shearman & Sterling,* New York City.

COMPLAINT

The Federal Trade Commission, having reason to believe that the party respondent named above, as hereinafter more particularly designated and described, has violated and is now violating the provisions of Section 7 of the Clayton Act (15 U.S.C. 18) and Section 5 of the Federal Trade Commission Act (15 U.S.C. 45), and it appearing to the Commission that a proceeding in respect thereof would be in the public interest, hereby issues its complaint pursuant to the provisions of Section 11 of the Clayton Act (15 U.S.C. 21) and Section 5 of the Federal Trade Commission Act (15 U.S.C. 45), stating its charges as follows:

DEFINITIONS

1. For the purpose of this complaint, the following definitions shall apply:

a. *Medical Laboratory Tests:* Tests or examinations performed on specimens drawn or otherwise taken from the human body, or on other organic material, for the purpose of assisting in the diagnosis of disease or assessment of medical condition or state of body condition; not including autopsies, x-ray and other radiographic examinations, and electrocardiographic and other electrographic examinations.

b. *Medical Laboratory Test Services:* The services performed by businesses performing or arranging for the performance of Medical Laboratory Tests in connection with the performance of such Tests, which services may include but are not limited to: provision of such equipment and supplies as are necessary to obtain specimens; pickup of specimens; performing or arranging for the performance of Medical Laboratory Tests; communication of results to interested parties; and giving assistance to physicians in their interpretation of the meaning of the results of said Medical Laboratory Tests.

c. *Independent Medical Laboratory:* Any establishment performing Medical Laboratory Tests and Services except for the following: any laboratory or laboratories maintained and operated by Federal, state, county or municipal government; any laboratory or laboratories maintained and operated solely for research or teaching purposes; any laboratory operated by a physician or medical group practice, provided such laboratory is operated solely in connection with the diagnosis and treatment of his own or the group's own patients; any laboratory maintained in a hospital and operated by a hospital; and any laboratory maintained and operated by any industrial organization, for the sole purpose of testing of specimens from its own employees.

d. *Metropolitan Philadelphia Area:* Philadelphia, Bucks, Montgomery, Chester and Delaware counties in the Commonwealth of Pennsylvania; and Gloucester, Camden and Burlington counties in the State of New Jersey.

e. *Metropolitan Chicago Area:* Cook, Lake, McHenry, Kane, DuPage and Will counties in the State of Illinois.

THE RESPONDENT

2. Respondent, Damon Corporation (hereinafter "Damon"), is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its principal office and place of business located at 115 Fourth Ave., Needham Heights, Massachusetts.

3. Damon is a manufacturer of electronic products. It also produces and sells educational materials, medical equipment, and medical supplies.

4. In 1969, Damon entered into a program of acquiring Independent Medical Laboratories with the purpose of assembling a nationwide chain of laboratories. Since that time Damon has made more than 50 acquisitions of Independent Medical Laboratories located and serving the public in the following geographic areas, among others: Anderson, South Carolina; Birmingham, Alabama; Bradenton, Florida; Metropolitan Chicago Area; Columbus, Missis-

sippi; Detroit, Michigan; Ft. Lauderdale, Florida; Huntsville, Alabama; Los Angeles, California; New York, New York; Orlando, Florida; Parkersburg, West Virginia; Metropolitan Philadelphia Area; Phoenix, Arizona; Santa Barbara, California; Tampa, Florida; Topeka, Kansas; Ventura, California; Washington, D. C. By 1974, Damon's network of Independent Medical Laboratories had become one of the largest in the world.

5. Damon's total annual sales have risen from $15,709,000 in fiscal 1968 to $141,311,000 in fiscal 1974. Damon's sales of Medical Laboratory Tests and Services have grown from zero in fiscal 1968 to more than $50 million in fiscal 1974, or 40 percent of total annual sales.

6. At all times relevant herein, Damon has been a corporation engaged in commerce within the meaning of the Clayton and Federal Trade Commission Acts.

COUNT I

7. The allegations of Paragraphs One through Six, inclusive, of this complaint are incorporated herein by reference.

LINE OF COMMERCE

8. For purposes of this Count, the relevant service market is the provision of Medical Laboratory Tests and Services by Independent Medical Laboratories. Such Laboratories fill a unique and critical role in the nation's health care delivery system by providing a wide variety of Medical Laboratory Tests and ancillary Services at competitive rates to physicians and other medical practitioners, to clinics, and to governmental, industrial, and other institutions which administer health care services. Independent Medical Laboratories also provide Medical Laboratory Tests and Services to hospitals and nursing homes which care for patients confined to such institutions. No other health care institution provides such a variety of Medical Laboratory Services for the benefit of the public at large.

9. The relevant geographic markets for purposes of this Count are the Metropolitan Philadelphia and Metropolitan Chicago Areas.

THE ACQUISITIONS

10. Damon has acquired the following Independent Medical Laboratories in the Metropolitan Philadelphia Area:

a. On April 10, 1969, Damon acquired substantially all of the assets and properties of Lawndale Laboratory Company (hereinafter "Lawndale"). Prior to and until April 10, 1969, Lawndale was a corporation organized, existing and doing business under the laws of the Commonwealth of Pennsylvania with its principal place of business located in Philadelphia, Pennsylvania. At the time of its acquisition, Lawndale was the second largest Independent Medical Laboratory in the Metropolitan Philadelphia Area.

b. On April 17, 1969, Damon acquired all of the outstanding capital stock of Rhodes Laboratories, Inc., d/b/a Medical Arts Laboratories (hereinafter "Rhodes"). Prior to and until April 17, 1969, Rhodes was a corporation organized, existing and doing business under the laws of the Commonwealth of Pennsylvania with its principal place of business located in Willow Grove, Pennsylvania. At the time of its acquisition, Rhodes was the largest Independent Medical Laboratory in the Metropolitan Philadelphia Area.

c. On July 12, 1969, Damon acquired all of the outstanding capital stock of Rosoff Laboratories, Inc. (hereinafter "Rosoff"). Prior to and until July 12, 1969, Rosoff was a corporation organized, existing and doing business under the laws of the Commonwealth of Pennsylvania with its principal place of business located in Philadelphia, Pennsylvania.

d. On August 5, 1969, Damon acquired substantially all of the assets and properties of Elmcon, Inc., d/b/a Northeast Medical Center Laboratory (hereinafter "Elmcon"). Prior to and until August 5, 1969, Elmcon was a corporation organized, existing and doing business under the laws of the Commonwealth of Pennsylvania with its principal place of business located in Philadelphia, Pennsylvania.

e. On September 30, 1969, Damon acquired substantially all of the assets and properties of Claude P. Brown Associates, Inc. (hereinafter "Brown"). Prior to and until September 30, 1969, Brown was a corporation organized, existing and doing business under the laws of the State of Delaware with its principal place of business located in Philadelphia, Pennsylvania.

f. On July 1, 1970, Damon acquired substantially all of the assets and properties of E. Philip Halpern & William Ball, co-partners d/b/a Park Laboratories (hereinafter "Park"). Prior to and until July 1, 1970, Park was a partnership organized, existing and doing business under the laws of the Commonwealth of Pennsylvania with its principal place of business located in Philadelphia, Pennsylvania.

g. On May 19, 1972, Damon acquired substantially all of the assets and properties of Pathology Consultants, Inc. (hereinafter "Pathcon"), and its subsidiary, KNS Laboratories, Inc. (hereinafter

"KNS"). Prior to and until May 19, 1972, Pathcon was a corporation organized, existing and doing business under the laws of the Commonwealth of Pennsylvania, with its principal place of business located in Narberth, Pennsylvania. KNS was a corporation organized, existing and doing business under the laws of the State of New Jersey, with its principal place of business located in Woodbury, New Jersey.

h. On April 2, 1973, Damon acquired assets of Biomedical Resources Corporation (hereinafter "BMR"), including substantially all of BMR's assets in the Metropolitan Philadelphia Area. Prior to and until April 2, 1973, BMR was a corporation organized, existing and doing business under the laws of the State of New York, with its principal place of business located in New York, New York.

11. As a consequence of these acquisitions, by 1973, Damon had acquired approximately a 33 percent share of the Independent Medical Laboratory service market in the Metropolitan Philadelphia Area, and had become by far the largest Independent Medical Laboratory in that Area. The four largest Independent Medical Laboratories in the Area provided approximately 55 percent of such services in the Area in 1973.

12. Damon has acquired the following Independent Medical Laboratories in the Metropolitan Chicago Area:

a. On December 7, 1970, Damon acquired substantially all of the assets and properties of Mason-Barron Pathology Laboratories, S. C. (hereinafter "Mason-Barron"). Prior to and until December 7, 1970, Mason-Barron was a corporation organized, existing and doing business under the laws of the State of Illinois, with its principal place of business located in Chicago, Illinois. At the time of its acquisition, Mason-Barron was the largest Independent Medical Laboratory in the Metropolitan Chicago Area.

b. On December 10, 1970, Damon acquired all of the outstanding capital stock of Pasco Medical Laboratories, Inc. (hereinafter "Pasco"). Prior to and until December 10, 1970, Pasco was a corporation organized, existing and doing business under the laws of the State of Delaware, with its principal place of business located in Hinsdale, Illinois. At the time of its acquisition, Pasco was the second largest Independent Medical Laboratory in the Metropolitan Chicago Area.

c. On December 10, 1973, Damon acquired substantially all of the assets and properties of Aurora Clinical Laboratory, Inc. (hereinafter "Aurora"). Prior to and until December 10, 1973, Aurora was a corporation organized, existing and doing business under the laws of the State of Illinois, with its principal place of business located in Aurora, Illinois.

d. On August 1, 1974, Damon acquired substantially all of the assets of Omega Medical Laboratories, Inc. (hereinafter "Omega"). Prior to and until August 1, 1974, Omega was a corporation organized, existing and doing business under the laws of the State of Illinois with its principal place of business located in Downers Grove, Illinois.

13. As a consequence of these acquisitions, by 1973, Damon had acquired approximately a 25 percent share of the Independent Medical Laboratory service market in the Metropolitan Chicago Area, and had become by far the largest Independent Medical Laboratory in that Area. The four largest Independent Medical Laboratories in the Area provided approximately 35 percent of such services in the Area in 1973.

COMMERCE

14. At all times relevant, Lawndale, Rhodes, Rosoff, Elmcon, Brown, Pathcon, BMR, Mason-Barron, Pasco, Aurora and Omega were corporations engaged in commerce, as that term is used in Section 7 of the Clayton Act, as amended, (15 U.S.C. 18), and in Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45). Park was a partnership, also engaged in commerce as that term is used in Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45). Each of these acquisitions affected commerce, as that term is used in Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45).

VIOLATIONS CHARGED

15. The effect of Damon's acquisitions of the stock and assets of Lawndale, Rhodes, Rosoff, Elmcon, Brown, Pathcon, and BMR in the Metropolitan Philadelphia Area, and of the stock and assets of Mason-Barron, Pasco, Aurora, and Omega in the Metropolitan Chicago Area, separately and cumulatively, may be substantially to lessen competition or to tend to create a monopoly in the Independent Medical Laboratory service market in the Metropolitan Philadelphia Area and in the Metropolitan Chicago Area in violation of Section 7 of the Clayton Act, as amended, (15 U.S.C. 18); and, the acquisitions by Damon of the stock and assets of the aforesaid corporations and Park, a partnership, separately and cumulatively, together with the subsequent use of such assets were and are to the prejudice and injury of the public and constitute unfair methods of

competition and unfair acts in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45); in the following ways, among others:

a. Actual competition and potential competition among and between the aforesaid corporations and partnership has been eliminated in the relevant markets.

b. Actual competition and potential competition between Damon and the aforesaid corporations and partnership has been eliminated in the relevant markets.

c. The trend toward concentration in the relevant markets has been accelerated.

d. The level of concentration in the relevant markets has been increased.

e. Damon has established itself as a dominant factor in the relevant markets by means of said acquisitions.

COUNT II

16. The allegations of Paragraphs One through Six, inclusive, of this complaint, are incorporated herein by reference.

RESPONDENT'S PRACTICES

17. In the course and conduct of its operation of Independent Medical Laboratories, Damon, through its subsidiaries and agents, has engaged in the practice, in various sections of the country, of making payments and/or granting other things of value, and/or causing intermediaries to make such payments and grants, to physicians and others ordering or arranging for Medical Laboratory Tests to be performed on behalf of patients by or through Damon or its subsidiaries. Said payments and grants, which were made during a period extending at least from 1971 until mid-1975, were intended by Damon and its subsidiaries to induce said persons to refer specimens, or to arrange for specimens to be referred, to Damon rather than its competitors, and to compensate said persons for so doing. More specifically, Damon has engaged in the following practices, among other things:

a. Damon has engaged in the practice of making payments, sometimes termed "handling fees" or "phlebotomy fees" and calculated either on the basis of a specific amount per test, or per specimen, or per patient, or as a specific amount per month, to physicians, and to nurses and other agents of physicians, to induce said persons and/or said physicians to arrange for submission of

Medical Laboratory Tests to Damon rather than to its competitors, and to compensate said persons for so doing.

b. Damon has also engaged in the practice of causing intermediaries to make payments of the type described in sub-paragraph (a), above, to physicians, to induce said physicians to arrange for submission of Medical Laboratory Tests to Damon rather than to its competitors, and to compensate said persons for so doing.

c. Damon has also engaged in the practice of making payments, equivalent to a percentage of amounts billed by or due to Damon for Medical Laboratory Tests submitted by physicians and medical clinics, to said physicians and to owners and managers of said medical clinics, and to their agents, to induce said persons to arrange for the submission of Medical Laboratory Tests to Damon rather than to its competitors, and to compensate said persons for so doing. In certain instances these payments have been termed "specimen collection fees," "handling fees," "rental fees," "maintenance fees" or "consultant fees."

d. Damon has also engaged in the practice of writing off charges and/or foregoing collection of all or part of amounts due from physicians for Medical Laboratory Tests to induce said physicians to refer Medical Laboratory Tests chargeable to patients and other parties to Damon rather than to its competitors, and to compensate said physicians for so doing.

e. Damon has also engaged in the practice of granting volume discounts to physicians with the intent that the benefit derived from said discounts would inure to said physicians, to induce said physicians to refer Medical Laboratory Tests to Damon rather than to its competitors, and to compensate said physicians for so doing.

VIOLATIONS CHARGED

18. The aforesaid acts and practices of Damon and its subsidiaries and agents have had the tendency unduly to restrict and restrain competition and have injured, hindered, suppressed, lessened or eliminated actual or potential competition, are to the prejudice and injury of the public, and constitute unfair methods of competition in or affecting commerce and unfair or deceptive acts and practices in or affecting commerce, in violation of Section 5 of the Federal Trade Commission Act (15 U.S.C. 45), for the following reasons, among others:

a. Physicians have been induced to order Medical Laboratory Tests on the basis of payments or things of value offered or received rather than on the basis of patients' welfare.

b. Physicians and others have been induced to refer Medical

Laboratory Tests on the basis of payments or things of value offered or received rather than on the basis of other factors, such as price, quality and/or service.

c. Laboratories making said payments have obtained unfair competitive advantage over their competitors.

d. The public has been deprived of accurate information concerning said acts and practices, and therefore has been rendered unable to evaluate the relative prices of Medical Laboratory Tests and other medical services on an informed basis.

e. As a consequence, certain Medical Laboratory Test prices have tended to be stabilized at higher levels, and overall costs to consumers have been increased.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and respondent having been furnished thereafter with a copy of a draft of complaint which the Bureau of Competition proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violations of Section 7 of the Clayton Act and of Section 5 of the Federal Trade Commission Act; and

The respondent and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having considered the agreement and having provisionally accepted same and placed it on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of the Commission's Rules, now in further conformity with the procedure provided by Section 2.34 of its Rules hereby issues its decision in disposition of the proceeding against the above-named respondent, makes the following jurisdictional findings, and enters the following findings and order:

1. Respondent Damon Corporation is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its executive offices located at 115 Fourth Ave., Needham Heights, Massachusetts.

2. The Federal Trade Commission has jurisdiction over the subject matter of this proceeding and over the respondent, and the proceeding is in the public interest.

ORDER

I

For purposes of this order, the following definitions shall apply:

1. *Respondent:* Damon Corporation, and those persons, partnerships, corporations, and other legal entities acting on its behalf, including but not limited to, its officers, directors, agents, representatives, employees, subsidiaries, affiliates, successors and assigns.

2. *Medical Laboratory Tests:* Tests or examinations performed on specimens drawn or otherwise taken from the human body, or on other organic material, for the purpose of assisting in the diagnosis of disease or assessment of medical condition or state of body condition; not including autopsies, x-ray and other radiographic examinations, and electrocardiographic and other electrographic examinations.

3. *Medical Laboratory Test Services:* The services performed by businesses performing or arranging for the performance of Medical Laboratory Tests in connection with the performance of such Tests, which services may include but are not limited to: provision of such equipment and supplies as are necessary to obtain specimens; pick-up of specimens; performing or arranging for the performance of Medical Laboratory Tests; communication of results of Medical Laboratory Tests to interested parties; and giving assistance to physicians in their interpretation of the meaning of the results of such Medical Laboratory Tests.

4. *Independent Laboratory:* any entity performing or arranging for the performance of Medical Laboratory Tests, other than a entity: (1) owned and operated by a hospital or hospitals; or (2) more than 90 percent of the Net Sales of Medical Laboratory Tests of which during its four most recent complete fiscal quarters were attributable to sales of Medical Laboratory Tests performed at said laboratory on specimens obtained from in-patients and out-patients of either: (i) a single hospital, or (ii) a group of hospitals that has jointly contracted to purchase Medical Laboratory Test Services from a single source or to have such Test Services performed by a single source.

5. *Net Sales:* gross sales minus returns, discounts and allowances.

II

A. *It is ordered,* That for a period of ten (10) years from the date of service of this order, respondent shall not acquire, directly or indirectly, without the prior approval of the Federal Trade Commission, the whole or any part of the stock, share capital, or any other indicia of ownership of, or any ownership interest in, any other Independent Laboratory: (1) which performs any Medical Laboratory Tests at any location within a Market; or (2) which during its four most recent fiscal quarters has derived more than twenty-five percent (25%) of its Net Sales of Medical Laboratory Tests from Tests performed upon specimens originating from within any one Market.

B. For purposes of this Part II, any arrangement between respondent and an Independent Laboratory pursuant to which such Independent Laboratory:

1. Transfers or otherwise makes available to respondent, for a consideration, any list of customers for Medical Laboratory Tests in a Market; or

2. Discontinues the solicitation of customers for, or the marketing of, Medical Laboratory Tests within a Market, pursuant to an understanding with respondent, and thereafter refers or sends customers for Medical Laboratory Tests in such Market to respondent;

shall constitute an acquisition by respondent of an ownership interest in such Independent Laboratory subject to the provisions of Paragraph A of this Part II.

C. For purposes of this Part II, the term "Market" shall mean each of the following geographic areas:

1. the Philadelphia, Pennsylvania area, being Bucks, Chester, Delaware, Montgomery and Philadelphia counties within the Commonwealth of Pennsylvania; and Burlington, Camden and Gloucester counties within the State of New Jersey;

2. the Chicago, Illinois area, being Cook, DuPage, Kane, Lake, McHenry and Will counties within the State of Illinois;

3. the Birmingham, Alabama area, being Jefferson, St. Clair, Shelby and Walker counties within the State of Alabama;

4. the Tampa, Florida area, being Hillsborough, Pasco and Pinellas counties within the State of Florida;

5. the Bradenton, Florida area, being Manatee County within the State of Florida;

6. the Phoenix, Arizona area, being Maricopa County within the State of Arizona;

7. the Orlando, Florida area, being Orange, Osceola and Seminole counties within the State of Florida;

8. the Huntsville, Alabama area, being Limestone, Madison and Marshall counties within the State of Alabama;

9. the Topeka, Kansas area, being Jefferson, Osage and Shawnee counties within the State of Kansas;

10. the Los Angeles, California area, being Los Angeles county within the State of California;

11. the Ventura, California area, being Ventura county within the State of California;

12. the Santa Barbara, California area, being Santa Barbara county within the State of California;

provided, that if respondent, in any of its fiscal years during the continuing existence of this Part II has less than five hundred thousand dollars ($500,000) in Net Sales of Medical Laboratory Tests performed on specimens originating from within any geographic area listed above, said area or areas shall not constitute a Market for each of respondent's subsequent fiscal quarters during which respondent's Net Sales of Medical Laboratory Tests performed on specimens originating from within said area or areas, including such sales by any Independent Laboratory acquired by respondent, are below one hundred and twenty-five thousand dollars ($125,000).

D. No acquisition made by respondent shall be deemed immune or exempt from the provisions of the antitrust laws by reason of anything contained in this order.

III

A. *It is further ordered*, That respondent shall not, directly or indirectly, make any payment of money, or grant or transfer any other thing of value, to or for the benefit of any person: (a) to induce such person either: (i) to contract with respondent for respondent to perform any Medical Laboratory Test Service; or (ii) to order or arrange for any Medical Laboratory Test Service to be performed by or through respondent; or (b) to compensate such person for so contracting, ordering, or arranging; whether or not said payment, grant or transfer is described or regarded as a rebate, credit, gift, commission, rental payment, participation in or share of profits, payment for any service in connection with the provision of any Medical Laboratory Test Service, or otherwise. This provision shall not, however, prohibit respondent:

(1) from providing Medical Laboratory Test Services to any person without charge, unless respondent knows or should know that such

person will receive anything of value for such Services from any other person or a hospital; or

(2) from granting such bona fide extensions of credit to persons charged for Medical Laboratory Test Services as are usual in the normal course of providing such Medical Laboratory Test Services; or

(3) from granting to persons charged for Medical Laboratory Test Services any discount or reduced price for any Medical Laboratory Test Services (free Medical Laboratory Test Services, however, being controlled solely by subparagraph (1) above and not by this subparagraph); *provided,* that subsequent to the date six (6) months after the date of service of this order upon respondent, (i) the resultant net price for each Medical Laboratory Test Service on which any discount or reduced price is granted is provided in writing to the person charged for the Medical Laboratory Test Services before or at the time said person is billed for such Services, and (ii) the method of calculation and the conditions of eligibility for such discount or reduced price are clearly stated in writing on all notices of charges therefor.

B. For the purposes of this Part III, the term "person" shall mean any individual, corporation, partnership, trust, unincorporated association or organization, or government or agency or political subdivision thereof, other than a hospital or respondent.

C. No act or practice carried out by respondent shall be deemed immune or exempt from the laws of any state or of the United States by reason of anything contained in this order.

IV

It is further ordered, That for a period of ten (10) years from the date of service of this order, respondent shall, within ten (10) days after signing an agreement in principle to acquire any Independent Laboratory, or after the acquisition of any Independent Laboratory, whichever event is first, submit the following information in writing to the Federal Trade Commission:

1. Name of such Independent Laboratory.

2. Location of each facility owned, operated, or managed by such Independent Laboratory at which Medical Laboratory Tests were performed within the twelve (12) month period preceding the date of notification and, with respect to each such facility:

a. Net Sales of Medical Laboratory Tests for each of the last twelve (12) complete fiscal quarters prior to the date of notification;

b. The principal geographic area(s) it served within the twelve (12) month period prior to the date of notification; and

c. Medical Laboratory Tests it was licensed to perform by any state or federal agency within the twelve (12) month period prior to the date of notification.

3. Price paid or to be paid for such Independent Laboratory.

4. Location of the facility owned, operated, or managed by respondent at which Medical Laboratory Tests were performed within the twelve (12) month period preceding the date of notification which was nearest to each facility of such Independent Laboratory identified pursuant to (2) above.

5. Net Sales of Medical Laboratory Tests attributable to each facility of respondent identified pursuant to (4) above for each of the last twelve (12) complete fiscal quarters of respondent prior to the date of notification.

6. Date of closing or contemplated date of closing.

V

It is further ordered, That respondent shall forthwith distribute a copy of this order to each of its operating divisions, its present corporate officers, its medical laboratory directors, and its sales personnel; and shall secure from each such officer, director, and employee, a signed statement acknowledging receipt of said order.

VI

It is further ordered, That respondent shall, within sixty (60) days after the date of service of this order, and thereafter on the first anniversary date of the date of service of this order and on each anniversary date thereafter to and including the tenth anniversary date, submit in writing to the Commission a report setting forth in detail the manner and form in which respondent intends to comply, is complying, and has complied with Parts II and III of this order. All compliance reports shall include such other information and documentation as may hereafter be required to show compliance with this order.

VII

It is further ordered, That respondent shall notify the Commission at least thirty (30) days prior to any proposed change in its corporate structure such as dissolution, assignment or sale resulting in the emergence of a successor corporation, or any other change in the corporation, which may affect obligations arising out of this order.

IN THE MATTER OF

GROLIER, INCORPORATED, ET AL.

ORDER, OPINION, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket 8879. Complaint, Mar. 9, 1972 — Final Order, Mar. 13, 1978.*

This order, among other things, requires a New York City publisher and seller of encyclopedia and other educational materials and services, and its subsidiaries to cease misrepresenting, failing to make relevant disclosures, or using any other unfair or deceptive method to recruit door-to-door sales personnel, sell merchandise and services, and collect delinquent accounts.

Appearances

For the Commission: *Edward D. Steinman, David C. Fix* and *Robert D. Friedman.*

For the respondents: *Frederick P. Furth, Thomas R. Fahrner* and *Robert C. Cagen, Furth, Fahrner & Wong,* San Francisco, Calif.

[2] COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Grolier, Incorporated, American Peoples Press, Inc., Americana Corporation, Americana Interstate Corp., Career Institute, Inc., Federated Credit Corp., Grolier Enterprises, Inc., Grolier Interstate, Inc., Grolier New Era Corp., Grolier Reading Programs, Inc., Madison Enterprises, Inc., R.H. Hinkley Company, Spencer International Press, Inc., The Grolier Society, Inc., and The Richards Company, Inc., corporations, hereinafter referred to as respondents, have violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent Grolier, Incorporated is a corporation organized, existing, and doing business under and by virtue of the laws of the State of Delaware, with its principal office and place of business located at 575 Lexington Ave., New York, New York.

Respondent Grolier, Incorporated dominates, controls, and furnishes the means, instrumentalities, services and facilities for, and condones and approves the acts and practices of the corporations hereinafter referred to below.

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* Complaint reported as amended by the administrative law judge's order of Jan. 10, 1973.

Respondent American Peoples Press, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Illinois, with its principal office and place of business located at Sherman Turnpike, Danbury, Connecticut. It is a wholly-owned subsidiary corporation of respondent Grolier, Incorporated and sells and distributes books or other merchandise through advertising and mailings. Its volume of business has been, and is substantial. [3]

Respondent Americana Corporation is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its principal office and place of business located at 575 Lexington Ave., New York, New York. It is a wholly-owned subsidiary corporation of respondent Grolier, Incorporated and recruits persons by means of various methods of advertising, as hereinafter set forth, and trains said persons to work as door-to-door sales personnel. It sells and otherwise distributes encyclopedias, yearbooks, and other publications, merchandise or services to the general public, through various methods, including door-to-door canvassing, as hereinafter set forth. Its volume of business has been, and is substantial.

Respondent Americana Interstate Corp. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Illinois, with its principal office and place of business located at 501 East Lange St., Mundelein, Illinois. It is a wholly-owned subsidiary corporation of respondent Grolier, Incorporated, and sells and distributes books or other merchandise through advertising and mailings. Its volume of business has been, and is substantial.

Respondent Career Institute, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Illinois, with its principal office and place of business located at 555 East Lange St., Mundelein, Illinois. It is a wholly-owned subsidiary corporation of respondent Grolier, Incorporated, and sells and distributes books or other merchandise through advertising and mailings. Its volume of business has been, and is substantial.

Respondent Federated Credit Corp. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its principal office and place of business located at 575 Lexington Ave., New York, New York. It is a wholly-owned subsidiary corporation of respondent Grolier, Incorporated, and collects and induces payment of accounts for the subsidiary corporations of respondent Grolier, Incorporated by various methods, as hereinafter set forth. Its volume of business has been, and is substantial. [4]

Respondent Grolier Enterprises, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York, with its principal office and place of business located at Sherman Turnpike, Danbury, Connecticut. It is a wholly-owned subsidiary corporation of respondent Grolier, Incorporated and sells and distributes books or other merchandise through advertising and mailings. Its volume of business has been, and is substantial.

Respondent Grolier Interstate, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its principal office and place of business located at 575 Lexington Ave., New York, New York. It is a wholly-owned subsidiary corporation of respondent Grolier, Incorporated and recruits persons by means of various methods of advertising, as hereinafter set forth, and trains said persons to work as door-to-door sales personnel. It sells and otherwise distributes encyclopedias, yearbooks, and other publications, merchandise or services to the general public, through various methods, including door-to-door canvassing, as hereinafter set forth. Its volume of business has been and is substantial.

Respondent Grolier New Era Corp. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Illinois, with its principal office and place of business located at 575 Lexington Ave., New York, New York. It is a wholly-owned subsidiary corporation of respondent Grolier, Incorporated, and recruits persons by means of various methods of advertising, as hereinafter set forth, and trains said persons to work as door-to-door sales personnel. It sells and otherwise distributes encyclopedias, yearbooks, and other publications, merchandise or services to the general public, through various methods, including door-to-door canvassing, as hereinafter set forth. Its volume of business has been, and is substantial. [5]

Respondent Grolier Reading Programs, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York, with its principal office and place of business located at Sherman Turnpike, Danbury, Connecticut. It is a wholly-owned subsidiary corporation of respondent Grolier, Incorporated, and sells and distributes books or other merchandise through advertising and mailings. Its volume of business has been, and is substantial.

Respondent Madison Enterprises, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of California, with its principal office and place of business located at 635 Madison Ave., New York, New York. It is a wholly-owned subsidiary corporation of respondent Grolier, Incorporated, and recruits persons by means of various methods of advertising, as hereinafter set forth, and trains said persons to work as door-to-door sales personnel. It sells and otherwise distributes encyclopedias, yearbooks, and other publications, merchandise or services to the general public, through various methods, including door-to-door canvassing, as hereinafter set forth. Its volume of business has been, and is substantial.

Respondent R. H. Hinkley Company is a corporation organized, existing and doing business under and by virtue of the laws of the State of Maine, with its principal office and place of business located at 575 Lexington Ave., New York, New York. It is a wholly-owned subsidiary corporation of respondent Grolier, Incorporated, and recruits persons by means of various methods of advertising, as hereinafter set forth, and trains said persons to work as door-to-door sales personnel. It sells and otherwise distributes encyclopedias, yearbooks, and other publications, merchandise or services to the general public, through various methods, including door-to-door canvassing, as hereinafter set forth. Its volume of business has been, and is substantial. [6]

Respondent Spencer International Press, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its principal office and place of business located at 575 Lexington Ave., New York, New York. It is a wholly-owned subsidiary corporation of respondent Grolier, Incorporated, and recruits persons by means of various methods of advertising, as hereinafter set forth, and trains said persons to work as door-to-door sales personnel. It sells and otherwise distributes encyclopedias, yearbooks, and other publications, merchandise or services to the general public, through various methods, including door-to-door canvassing, as hereinafter set forth. Its volume of business has been, and is substantial.

Respondent The Grolier Society, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its principal office and place of business located at 575 Lexington Ave., New York, New York. It is a wholly-owned subsidiary corporation of respondent Grolier, Incorporated, and recruits persons by means of various methods of advertising, as hereinafter set forth, and trains said persons to work as door-to-door sales personnel. It sells and otherwise distributes encyclopedias, yearbooks, and other publications, merchandise or services to the general public through various methods, including door-to-door canvassing, as hereinafter set forth. Its volume of business has been, and is substantial.

Respondent The Richards Company, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its principal office and place of business located at 635 Madison Ave., New York, New York. It is a wholly-owned subsidiary corporation of respondent Grolier, Incorporated, and recruits persons by means of various methods of advertising, as hereinafter set forth, and trains said persons to work as door-to-door sales personnel. It sells and otherwise distributes encyclopedias, yearbooks, and other publications, merchandise or services to the general public, through various methods, including door-to-door canvassing, as hereinafter set forth. Its volume of business has been, and is substantial. [7]

PAR. 2. Respondent Grolier, Incorporated through its various organizational divisions and wholly-owned subsidiary corporations publishes, sells and otherwise distributes, throughout the world, textbooks, encyclopedias, reference or educational materials, training courses and teaching machines, or other publications, merchandise or services. It has established, acquired and operated a number of wholly-owned corporate subsidiaries as aforesaid, for the purpose of promoting, selling, or otherwise distributing, and collecting monies expended for said publications, merchandise or services from the trade or from the purchasing public. Its volume of business has been, and is substantial. In addition, respondent Grolier, Incorporated, directly and indirectly, profits and benefits by and through the acts and practices of its wholly-owned subsidiaries, including the acts and practices hereinafter set forth.

PAR. 3. In the course and conduct of their business, as aforesaid, respondents now cause, and for some time last past have caused, said publications, merchandise or services to be shipped and distributed from their places of business or from their sources of supply to purchasers and prospective purchasers thereof located in various States of the United States other than the state of origination, distribution or storage of said publications, merchandise or services. Respondents transmit and receive, and cause to be transmitted and received, invoices, checks, collection notices and various other commercial papers or documents in the course of advertising, selling, or otherwise distributing and collecting payment for said publications, merchandise or services among and between the several States of the United States. Respondents maintain, and at all times mentioned herein have maintained, a substantial course of trade in such publications, merchandise or services in commerce, as "commerce" is defined in the Federal Trade Commission Act. [8]

COUNT I

Alleging violation of Section 5 of the Federal Trade Commission Act, the allegations of Paragraphs One, Two and Three hereof are incorporated by reference in Count I with respect to respondents Grolier, Incorporated, and its wholly-owned subsidiaries Americana Corporation, Grolier Interstate, Inc., Grolier New Era Corp., Madison Enterprises, Inc., R. H. Hinkley Company, Spencer International Press, Inc., The Grolier Society, Inc., and The Richards Company, Inc., as if fully set forth verbatim:

PAR. 4. In the course and conduct of their business, and for the purpose of recruiting persons for door-to-door solicitations, respondents disseminate advertisements in various publications of general circulation which contain statements concerning the nature of the advertised positions. In addition, during subsequent interviews with persons responding to said advertisements, respondents and their representatives or agents provide further details concerning the type of positions and the method of payment of persons engaged in such positions. Through the use of the aforesaid advertisements and by oral statements of respondents and their representatives or agents, respondents have represented, directly or by implication that:

1. Respondents are offering positions in such fields as "market research analysis," "public relations" or other non-selling fields.
2. Respondents are offering to train persons as "management trainees," "junior executives" or other positions of responsibility concerned principally with administrative office functions. [9]
3. Respondents are offering persons a guaranteed weekly or monthly salary in excess of $100 per week or in excess of $350 to $500 per month, or other similar salaries.
4. Persons engaged by respondents contact other persons in their homes or places of business primarily for the purposes of conducting surveys, advertising promotions or for other non-selling purposes.

PAR. 5. In truth and in fact:

1. Respondents are not offering positions in the fields represented. To the contrary, respondents are recruiting persons, in the main, as salesmen and saleswomen in the door-to-door sale of respondents' publications, merchandise or services.
2. Respondents will not train persons for the positions represented. Persons hired by respondents are sent out to sell and are not trained to conduct administrative functions in an office.

3. Respondents do not, in all instances, reimburse persons in the amounts or in the manner represented. Due to the conditions or limitations imposed upon such persons, few if any, receive the guaranteed salary. Furthermore, respondents, in some instances, refuse to permit persons to be engaged under any arrangement other than a pure commission basis.

4. Persons engaged by respondents do not contact prospects in their homes or places of business primarily for the purposes represented by respondents. Such persons, in most instances, canvass neighborhoods in an attempt to solicit orders for respondents' publications, merchandise or services. [10]

Therefore, the statements, representations, acts and practices set forth in Paragraphs Four and Five hereof were and are unfair, and false, misleading and deceptive.

PAR. 6. In the course and conduct of their business as aforesaid, and for the purpose of inducing members of the general public to purchase respondents' publications, merchandise or services, respondents through their sales representatives utilize various forms of promotional materials in conjunction with oral sales presentations containing statements concerning the purpose of the initial contact with the prospect, the identity of the solicitor, the nature of the offer and the terms of respondents' contracts or other agreements. In the foregoing manner, respondents and their sales representatives have represented, directly or by implication, that:

1. Respondents' sales representatives are contacting persons in their homes or places of business primarily for the purpose of conducting a survey, or a brand identification analysis relating to the marketing of respondents' publications, merchandise or services, or for purposes other than the sale of such merchandise.

2. Respondents' sales representatives will take only a few minutes to complete their presentations inside prospects' homes or places of business.

3. Persons contacted by respondents' sales representatives have been specially selected to receive respondents' offers.

4. Respondents are offering certain of their publications, merchandise or services without cost to persons agreeing to do any one or more of the following acts or similar acts:

a. Display the publications in a conspicuous location in their homes;

b. Write a letter evaluating the merits of the publications which may be used in advertising; [11]

c. Provide respondents with the names of persons interested in purchasing respondents' publications;

d. Keep the publications current by purchasing respondents' yearbooks for a 10-year period or by purchasing respondents' Fact Research Service for 10 years;

e. Complete all installment payments for publications, merchandise or services, other than the publications, merchandise or services provided without cost, in a period less than 10 years; and

f. Pay a membership fee in order to participate in the Consumer Buying Educational Service which provides an opportunity for participants to purchase merchandise at a savings from the general retail prices for such merchandise.

5. The encyclopedias being offered by respondents' sales representatives to prospects are new publications; are publications which have not been previously available to the general public; or are editions which contain substantial editorial revisions from prior editions of the same publications.

6. Persons who purchase respondents' publications, in combination with other publications will realize a significant savings from the stated higher prices at which such publications have been sold by respondents in substantial quantities to the general public.

7.* The claimed retail prices of their publications are the prices at which such publications have been sold by respondents in substantial quantities to the general public. [12]

8. The various offers made available to prospects are of limited duration and prospects will not be given another opportunity to accept such offers.

9. Respondents' publications, merchandise or services have, in each instance when so represented, received bona fide endorsements or recommendations in the recent past from Better Business Bureaus, or from educational, religious, private or governmental institutions or from private persons.

10. Respondents provide financial terms to purchasers of their publications, merchandise or services such as annual payments for "10 years" or payments of "10¢ per day."

11. Persons subscribing to respondents' Fact Research Service receive answers to questions regarding any subject.

12. The answers provided by respondents' Fact Research Service are the product of detailed, exhaustive or original research generated by the specific questions asked by subscribers to said Service.

13. The answers provided by respondents' Fact Research Service can be used as suitable or acceptable substitutes for term papers, themes or other reports that may be required of students.

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* Published as amended by the ALJ's order of Jan. 10, 1973.

14. All answers, supplied by respondents to subscribers to the Fact Research Service, will arrive within a few days after the date of submission of the subscribers' questions.

Par. 7. In truth and in fact:

1. Respondents' sales representatives are not contacting persons in their homes or places of business primarily for the purpose of conducting a bona fide [13] survey, or a brand identification analysis relating to the marketing of respondents' publications, merchandise or services. To the contrary, the principal purpose for contacting such persons is to sell respondents' publications, merchandise or services.

2. Respondents' sales representatives do not ordinarily complete their presentations inside prospects' homes or places of business within only a few minutes. In actuality, a completed sales presentation frequently requires several hours.

3. Persons contacted by respondents' sales representatives have not been specially selected. Respondents, in fact, offer and sell their publications, merchandise or services to all members of the general public on a regular basis.

4. Respondents are not offering certain of their publications, merchandise or services without cost to any person who agrees to any one or more of the conditions set forth in Paragraph Six, subparagraph 4 herein. To the contrary, such conditions are not bona fide. Respondents, in many instances, do not require strict adherence to the agreed conditions. Furthermore, such conditions are used in an attempt to confuse persons into the erroneous belief that the amount of their monetary obligations to respondents does not include the cost of all the publications, merchandise or services obtained from respondents.

5. The encyclopedias being offered by respondents' sales representatives to prospects are not new publications. Such encyclopedias have been marketed to the general public for many years. Furthermore, in some instances, the only changes from earlier editions are minor editorial revisions. [14]

6. Persons who purchase respondents' publications in combination with other publications will not realize a significant savings from the stated higher prices at which such publications have been sold by respondents in substantial quantities to the general public. To the contrary, respondents have made only isolated or insignificant sales at the stated higher prices.

7.* The claimed retail prices of respondents' publications are not the prices at which such publications have been sold by them in substantial quantities to the general public. Furthermore, respondents have made only isolated or insignificant sales at the represented retail prices.

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* Published as amended by the ALJ's order of Jan. 10, 1978.

8. The various offers made available to prospects are not of limited duration and prospects, in most instances, can receive other opportunities to accept such offers.

9. Respondents' publications, merchandise or services have not, in each instance when so represented, received bona fide endorsements or recommendations in the recent past from Better Business Bureaus, or from educational, religious, private or governmental institutions or from private persons.

10. Respondents do not provide financial terms to purchasers of their publications, merchandise or services as represented. To the contrary, respondents, in most instances, require monthly installment payments of amounts which are substantially greater than "10¢ per day" or require payments to be made within a time period less than "10 years." [15]

11. Persons subscribing to respondents' Fact Research Service do not receive answers to questions regarding all subjects. To the contrary, respondents do not, in most instances, provide answers to questions concerning such subjects as medical, legal or financial matters.

12. The answers provided by respondents' Fact Research Service are not the product of detailed, exhaustive or original research generated by the specific question asked by the subscriber to said Service. For the most part, such answers are form responses containing general information not related to the specific inquiry.

13. The answers provided by the Fact Research Service, in most instances, are not suitable or acceptable substitutes for term papers, themes or reports that may be required of students.

14. The answers, supplied by respondents to subscribers to the Fact Research Service, in many instances, do not arrive within the period of time represented.

Therefore, the statements, representations, acts and practices set forth in Paragraphs Six and Seven hereof were and are unfair, and false, misleading and deceptive.

PAR. 8. In the further course and conduct of their business, respondents have conducted various contests and utilized other promotional devices for the purpose of obtaining leads to persons who will allow respondents' sales representatives into said persons' homes or for the purpose of inducing said persons to attend meetings held by respondents. The inducements used to achieve the above purposes are purportedly free merchandise, receipt of informational brochures obtained upon return of reply cards contained in promotional material, gift certificates entitling recipients to all expense paid vacations at resorts of their choice or other valuable considerations. [16]

Persons who enter any such contest, or who receive informational brochures, or who are told that they have been awarded a valuable gift are not informed by respondents of the material fact that as a result of entering the contest, receiving the informational brochures, or as a prerequisite to receiving a valuable gift or award, such persons will be subjected to a lengthy sales presentation for respondents' publications, merchandise or services. In many instances, such persons would not have accepted such inducements if respondents' actual purpose had been made known.

In addition, respondents have misrepresented the actual value of the aforesaid gift certificates. Persons are led into the erroneous belief that the certificates will enable such persons to have an all expense paid vacation at a resort of their choice. Respondents fail to advise such persons that the certificates do not include expenses such as transportation and meals. Such limitations and other restrictions imposed on the use of the certificates severely limit their actual value.

Therefore, the statements, representations, acts and practices, and the failure to disclose material facts as aforesaid were and are unfair and false, misleading and deceptive.

PAR. 9.* In the further course and conduct of their business, and for the primary purpose of promoting the sale of their encyclopedias or similar publications or services, respondents, through their sales representatives have utilized programs or other promotional selling devices which appeal to the emotional concerns of individuals for their own educational or intellectual development or of parents for the proper educational development of their children.

Through the use of "The Child Development Program," the "New Era Young Mothers Club," and "Programmed Learning" or other similar programs, [17] respondents' sales representatives contact prospects with young children and falsely represent, directly or by implication, that said programs or devices will provide tangible or intangible educational benefits or services such as periodic teaching guides designed to meet each child's educational or academic needs, or periodic questionnaires evaluating the child's progress in the claimed educational program.

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* Published as amended by the ALJ's order of Jan. 10, 1973.

By appealing to the emotional concerns of said persons through the use of false representations, as aforesaid, respondents persuade said persons to purchase respondents' publications, merchandise or services based on the aforesaid false representations of respondents, in some instances, confuse, confound or mislead such persons as to the purpose of said programs or devices which is to promote the sale of respondents' encyclopedias or similar publications or services in the regular course of respondents' business.

Therefore, the statements, representations, acts and practices as aforesaid, were and are false, misleading, deceptive and unfair.

COUNT II

Alleging violation of Section 5 of the Federal Trade Commission Act, the allegations of Paragraphs One, Two and Three hereof are incorporated by reference in Count II with respect to respondents Grolier, Incorporated and its wholly-owned subsidiaries American Peoples Press, Inc., Americana Corporation, Americana Interstate Corp., Career Institute, Inc., Federated Credit Corp., Grolier Interstate, Inc., Grolier New Era Corp., Madison Enterprises, Inc., R.H. Hinkley Company, Spencer International Press, Inc., The Grolier Society, Inc., and The Richards Company, Inc., as if fully set forth verbatim:

PAR. 10. In the further course and conduct of their business and for the purpose of collecting debts allegedly due and owing respondents pursuant to contracts or other agreements relating to the purchase of respondents' publications, merchandise or services, respondents and their representatives or agents, in numerous instances, have attempted to induce payment of accounts, either due or delinquent as the case may be, by the sending of dunning letters, [18] notices or similar instruments in the United States mail which contain statements and representations in the form of harassment or threats, including but not limited to the representations set forth below. Through such means, respondents have represented to the aforesaid members of the public, directly or indirectly, that:

(a) The respondent companies sending such instruments are divided into separate bona fide functional departments or divisions such as collection departments or legal departments.

(b) Employees of the federal government who fail to pay debts are subject to dismissal from federal service pursuant to the Civil Service Code of Federal Regulations.

(c) Purchasers of respondents' publications or services who utilize the United States mail to obtain such items and who fail to pay respondents or become delinquent in paying respondents are subject to prosecution for mail fraud under federal law.

(d) The respondents utilize the services of collection agencies, credit reporting companies or attorneys who disseminate credit information in a manner which will adversely affect the public or general credit rating of persons who have become delinquent in paying debts owed respondents.

(e) Letters or notices on the letterheads of attorneys or credit reporting companies are prepared or mailed by those individuals or concerns. [19]

(f) Respondents regularly transfer accounts to attorneys with instructions to institute suit or to take other legal steps to collect an outstanding debt.

PAR. 11. In truth and in fact:

(a) The respondent companies sending such instruments do not in each instance when so represented, have separate bona fide functional departments or divisions such as collection departments or legal departments.

(b) The Civil Service Code of Federal Regulations does not provide that federal employees are subject to dismissal from federal service for failure to pay outstanding debts. To the contrary, federal employees will not ordinarily be subject to dismissal unless it is demonstrated that the debt is just and the employee, after repeated attempts to arrange a satisfactory method of payment of the debt, has failed to pay said debt.

(c) Persons who have become delinquent in paying debts to respondents for publications or services received or ordered through the mail are not ordinarily prosecuted for mail fraud under federal law.

(d) The respondents, in some instances, do not utilize the services of collection agencies, credit reporting companies or attorneys who disseminate credit information in a manner which will adversely affect the public or general credit rating of persons who have become delinquent in paying debts owed respondents. [20]

(e) The letters or notices on the letterheads of attorneys or credit reporting companies are not prepared or mailed by said individuals or concerns. Said letters or notices are prepared or mailed, in many instances, by respondents. Replies or responses to said such mailings are forwarded unopened to respondents.

(f) Respondents do not regularly transfer accounts to attorneys with instructions to institute suit or to take other legal steps to collect outstanding debts.

Therefore, the statements and representations set forth in Paragraph Ten hereof were and are false, misleading and deceptive.

COUNT III

Alleging violation of Section 5 of the Federal Trade Commission Act, the allegations of Paragraphs One, Two and Three hereof are incorporated by reference in Count III with respect to respondents Grolier, Incorporated and its wholly-owned subsidiaries, American Peoples Press, Inc., Americana Interstate Corp., Inc., Career Institute, Inc., Grolier Enterprises, Inc. and Grolier Reading Programs, Inc., as if fully set forth verbatim:

PAR. 12. In the course and conduct of their business, respondents have and are disseminating advertisements in various publications of general circulation or in promotional materials mailed to members of the general public. By and [21] through such advertisements, respondents attempt to induce persons to become subscribers to continuity book promotion programs. A continuity book promotion program is a procedure whereby persons receive a single book on an approval basis. The aforesaid advertisements place emphasis on shipment of books, singly at intervals, without containing the material disclosure that all but a few of the books are mailed to subscribers by means of a bulk shipment. Among and including the statements and representations set forth in said advertisements, but not all inclusive thereof, are the following:

Step-Up Book Program

Accept your free book today. There's no obligation! When the book arrives, turn it over to your child and watch his reaction. If he's as pleased as I think he'll be, fine and dandy. You'll then be entitled to receive as many (or as few) additional STEP-UP BOOKS as you please, for the modest price of $1.65 each, plus delivery. Books will be sent to you on *approval*, and you'll have 10 days to decide whether to keep a book or return it at my expense.

Companion Library

As a subscriber to the Companion Library you are not obligated to take any minimum number of selections—take as many as you wish, or none at all, and cancel your membership whenever you like by mailing any invoice with the simple word "CANCEL" written across it.

Dandelion Library

Your free Twin Book edition of PETER PAN and ALICE IN WONDERLAND is your introduction to this delightful and important program. It is also the first in a series of exciting DANDELION LIBRARY Twin Books that you and your child will greet with real pleasure—and sample without risk or obligation at our expense.

PAR. 13. Through the use of said statements or others of similar import and meaning but not specifically set forth herein, respondents have represented, and are continuing to represent, directly or by implication: [22]

(a) That subscribers to respondents' continuity programs are accorded the option of receiving a single book at a time, and thereby are afforded the opportunity to receive and review on approval each book separately, and to reject or accept same, until the expiration of the continuity program.

(b) That no further volumes of books will be received after said subscribers notify respondents to cancel their subscriptions to the programs.

(c) That persons who subscribe to respondents' continuity programs do so without risk or obligation.

PAR. 14. In truth and in fact:

(a) Subscribers to respondents' continuity programs are not accorded the option of receiving a single book at a time, and thereby are not afforded the opportunity to receive and review on approval each book separately, and to reject or accept same, until expiration of the continuity programs. Respondents do not advise subscribers of the material fact, when the subscribers initially receive promotional materials concerning the continuity programs, that all but the first several books are shipped in mass by means of single bulk shipments. Furthermore, respondents, in some instances, have refused to continue shipping a single volume at a time when so requested by subscribers.

(b) Subscribers to respondents' continuity programs, in many instances, continue to receive volumes of books after notifying respondents to cancel their subscriptions to the programs. [23]

(c) Subscribers to respondents' continuity programs are subject to risks or obligations. Once a person subscribes to the continuity programs, respondents impose the following duties or obligations on the subscribers: must notify respondents to prevent shipment of additional books; must return to respondents all books found unacceptable; must pay for all books not returned to respondents. Subscribers also incur the risk that due to delays in mail delivery or computer error they will receive unordered merchandise or incorrect billings in the manner set forth in Paragraph Fifteen hereinafter.

Therefore, respondents' statements, representations, acts and practices, and their failure to disclose material facts, as set forth in Paragraphs Twelve through Fourteen hereof, were and are, false, misleading, deceptive and unfair.

PAR. 15. In the further course and conduct of their business, respondents have attempted to promote the sale of substantial quantities of their publications through the manner and form set forth in Paragraph Twelve hereof. Respondents' material alteration of the conditions and terms of the continuity programs, as initially represented, from shipment of a single book at intervals to shipment of all the books in mass, places an unfair and undue burden on subscribers to notify respondents affirmatively in order to prevent shipment of books not expressly authorized by said subscribers. Furthermore, respondents have, in numerous instances, shipped the books in mass after subscribers have notified respondents within a reasonable time that the altered method of distribution was unacceptable. As a result of the unwanted, unauthorized mass shipment of books, subscribers have expended their time or energies to dispose of the books sent to them.

In addition, such subscribers are subject to repeated and unrelenting mailings of bills, dunning letters and the like for unwanted, unordered [24] merchandise which, in many instances, has been previously returned to respondents. It is evident that respondents' bulk method of distribution, as aforesaid, attempts to or has the effect of causing the purchase of respondents' books in a manner and quantity not contemplated by subscribers when the continuity programs were first offered by respondents.

Therefore, the acts and practices as aforesaid, were and are, unfair and false, misleading and deceptive.

COUNT IV

Alleging violation of Section 5 of the Federal Trade Commission Act, the allegations of Paragraphs One through Fifteen hereof are incorporated by reference in Count IV with respect to respondents Grolier, Incorporated and its wholly-owned subsidiaries American Peoples Press, Inc., Americana Corporation, Americana Interstate Corp., Career Institute, Inc., Federated Credit Corp., Grolier Enterprises, Inc., Grolier Interstate, Inc., Grolier Reading Programs, Inc., Madison Enterprises, Inc., Grolier New Era Corp., R. H. Hinkley Company, Spencer International Press, Inc., The Grolier Society, Inc., and The Richards Company, Inc., as if fully set forth verbatim:

PAR. 16. In the course and conduct of their business, and at all times mentioned herein, respondents have been, and now are, in substantial competition, in commerce, with corporations, firms and individuals in the sale of publications, merchandise and services of the same general kind and nature as that sold by respondents.

PAR. 17. The use by respondents of the aforesaid unfair and false, misleading and deceptive statements, representations and practices, and their failure to disclose material facts, as [25] alleged in Counts I through III, has had, and now has, the capacity and tendency to mislead members of the public into the erroneous and mistaken belief that said statements and representations were, and are, true and complete, or into the purchase or retention of, and payment for substantial quantities of said publications, merchandise and services by reason of said erroneous and mistaken belief.

PAR. 18. The aforesaid acts and practices of respondents, as herein alleged, were and are all to the prejudice and injury of the public and of respondents' competitors and constituted, and now constitute, unfair methods of competition in commerce and unfair and deceptive acts and practices in commerce in violation of Section 5 of the Federal Trade Commission Act.

Chairman Kirkpatrick did not participate.

INITIAL DECISION BY THEODOR P. VON BRAND, ADMINISTRATIVE LAW JUDGE

OCTOBER 12, 1976

PRELIMINARY STATEMENT

The Commission issued a complaint on March 9, 1972, charging Grolier, Incorporated and 14 of its subsidiaries with violation of Section 5 of the Federal Trade Commission Act in connection with the sale of encyclopedias and other reference or educational materials, products or services. Respondents' answers denied the material allegations of the complaint.

Count I charges that Grolier, Incorporated and its wholly-owned direct selling subsidiaries have misrepresented: [2]

1. The nature of the positions and the compensation to be paid in connection therewith to prospective sales representatives;
2. The nature and purpose of consumer contacts;
3. The length of time a complete sales presentation will take in a prospective customer's home;
4. That prospective customers have been specially selected to receive respondents' offer;
5. That certain publications, merchandise or services are to be made available without cost if prospective customers agree to perform certain acts as, for example, to display the merchandise in a conspicuous place in their homes, write evaluation letters, furnish the names of other prospects or keep such publications current by

purchase of respondents' yearbooks or Fact Research Service for 10 years;

6. That the encyclopedias offered for sale are new or substantially revised editions;

7. That the claimed retail prices are the prices at which their publications have been sold in substantial quantities to the public;

8. That the offers made available to prospective customers are of limited duration;

9. That their merchandise had received certain bona fide endorsements;

10. The nature of the financial terms available;

11. The subject matter limitations on the Fact Research Service;

12. That the answers provided by the Fact Research Service are the product of detailed, exhaustive or original work generated by the subscriber's request; [3]

13. That Fact Research answers can be used as acceptable term papers, themes or other reports required of students; and

14. The time within which the Fact Research Service will respond to inquiries.

The complaint under this Count also charges as deceptive, respondents' use of contests or other promotional devices as a means of obtaining leads to prospective customers. It is alleged that there has been no disclosure that by participating therein, a customer will subject himself to a lengthy sales presentation.

Finally, Count I charges that, through the use and misrepresentation of programs such as "The Child Development Program," respondents have appealed to the emotional concerns of parents for their children and have misled customers as to the purpose of such programs, which is to promote the sale of encyclopedias or similar publications in the regular course of business.

Count II charges various unfair, deceptive and misleading acts and practices in connection with debt collection procedures.

Count III relates to the mail order operations. It alleges that respondents have misrepresented that subscribers to their continuity programs have the opportunity of receiving a single book at a time, with the option of receiving and reviewing each book separately until expiration of the continuity program; that no further volumes will be received after respondents have been notified by subscribers of their intention to cancel; and that persons who subscribe to the continuity program do so without risk or obligation. The complaint alleges in this connection that the subscribers are not initially advised of the material fact that all but the first several volumes are shipped in a bulk shipment. This Count concludes with the allegation that "respondents' bulk method of distribution. . . attempts to or has the effect of causing the purchase of respondents' books in a manner and quantity not contemplated by subscribers when the continuity programs were first offered by respondents." [4]

The administrative law judge originally assigned to this proceeding supervised the pretrial hearings and presided over the evidentiary hearings up to his retirement in December 1974. His successor recused himself at respondents' request, and the case was assigned to the undersigned in February 1975. Much of the case was reheard in view of respondents' contention that the demeanor evidence of witnesses previously appearing had to be preserved. The record was closed on May 14, 1976.

This initial decision is based upon the entire record* including proposed findings of fact and conclusions of law and briefs and supporting memoranda filed by the parties, as well as their responses. The undersigned has also taken into account his observation of the witnesses who appeared before him and their demeanor. Proposed findings not herein adopted, either in the form submitted or in substance, are rejected either as not supported by the evidence or as involving immaterial matters.

FINDINGS OF FACT

I. IDENTITY OF RESPONDENTS AND THE NATURE OF THEIR BUSINESS

1. Respondent Grolier, Incorporated (Grolier, Inc.) is a corporation organized, existing, and doing business under and by virtue of the laws of the State of Delaware, with its principal office and place of business located at 575 Lexington Ave., New York, New York (Complaint, ¶ One; ¶ Two, Ans. of Grolier, Inc.). Respondent Grolier, Inc. publishes, sells and otherwise distributes textbooks, encyclopedias, reference or educational materials, training courses, teaching machines, and other publications, merchandise, and services (Complaint, ¶ Two; ¶ 20, Ans. of Grolier, Inc.). Its volume of business has been, and is, substantial (¶ 22, Ans. of Grolier, Inc.).

2. Respondent American Peoples Press, Inc. (American Peoples Press) is a wholly-owned corporate subsidiary of Grolier, Inc. (Complaint, ¶ One; ¶ 2, Ans. of American Peoples Press). Respondent American Peoples Press is a corporation organized under the laws of the State of Illinois (Complaint, [5] ¶ One; ¶ 2, Ans. of American

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* Certain portions of the record were stricken where a witness ordered recalled did not appear or where the record of the recall hearings duplicated that compiled under the first administrative law judge.

Peoples Press). Its principal office and place of business was in Mundelein, Illinois (Tr. 16678–79). American Peoples Press sold and distributed books and other merchandise through advertising and mailings (Complaint, ¶ One; ¶ 2, Ans. of American Peoples Press). American Peoples Press ceased doing business by December 23, 1974 (Tr. 16679, 16711). Its volume of business has been substantial (¶ 2, Ans. of American Peoples Press).

3. Respondent Americana Interstate Corporation (Americana Interstate) is a wholly-owned corporate subsidiary of Grolier, Inc. (Complaint, ¶ One; ¶ 2, Ans. of Americana Interstate). Respondent Americana Interstate is a corporation organized under the laws of the State of Illinois (Complaint, ¶ One; ¶ 2, Ans. of Americana Interstate). Its principal office and place of business was at 501 East Lange St., Mundelein, Illinois (Tr. 16678–79). Americana Interstate sold and distributed books and other merchandise through advertising and mailings (Complaint, ¶ One; ¶ 2, Ans. of Americana Interstate). Americana Interstate ceased doing business by December 23, 1974 (Tr. 16679, 16711). Its volume of business has been substantial (¶ 2, Ans. of Americana Interstate).

4. Respondent Career Institute, Inc. (Career Institute) is a wholly-owned corporate subsidiary of Grolier, Inc. (Complaint, ¶ One; ¶ 2, Ans. of Career Institute). Respondent Career Institute is a corporation organized under the laws of the State of Illinois (Complaint, ¶ One; ¶ 2, Ans. of Career Institute). Its principal office and place of business was at 555 East Lange St., Mundelein, Illinois (Tr. 16678–79). Career Institute sold and distributed books through advertising and mailings (Complaint, ¶ One; ¶ 2, Ans. of Career Institute). Career Institute ceased doing business by December 23, 1974 (Tr. 16679, 16711). Its volume of business has been substantial (¶ 2, Ans. of Career Institute).

5. Respondent Grolier Enterprises, Inc. (Grolier Enterprises) is a wholly-owned corporate subsidiary of Grolier, Inc. (Complaint, ¶ One; ¶ 2, Ans. of Grolier Enterprises). Respondent Grolier Enterprises is a corporation organized, existing and doing business under the laws of the State of New York (Complaint, ¶ One; ¶ 2, Ans. of Grolier Enterprises). Its principal office and place of business is at Sherman [6] Turnpike, Danbury, Connecticut (Complaint, ¶ One; ¶ 2, Ans. of Grolier Enterprises). Grolier Enterprises sells and distributes books through advertising and mailings (Complaint, ¶ One; ¶ 2, Ans. of Grolier Enterprises; Tr. 16661). Its volume of business has been, and is, substantial (¶ 2, Ans. of Grolier Enterprises).

6. Respondent Grolier Reading Programs, Inc. (Grolier Reading Programs) is a wholly-owned corporate subsidiary of Grolier, Inc.

(Complaint, ¶ One; ¶ 2, Ans. of Grolier Reading Programs). Grolier Reading Programs is a corporation organized under the laws of the State of New York (Complaint, ¶ One; ¶ 2, Ans. of Grolier Reading Programs). Its principal office and place of business was at Sherman Turnpike, Danbury, Connecticut (Complaint, ¶ One; ¶ 2, Ans. of Grolier Reading Programs). Until 1971, Grolier Reading Programs sold and distributed books through advertising and mailings (Complaint, ¶ One; ¶ 2, Ans. of Grolier Reading Programs; Tr. 16643). Grolier Reading Programs has made no mailings on continuity book programs since the late summer of 1971 (Tr. 16644). Its volume of business has been substantial (¶ 2, Ans. of Grolier Reading Programs).

7. Respondent Americana Corporation (Americana) is a wholly-owned corporate subsidiary of respondent Grolier, Inc. (Complaint, ¶ One; ¶ 2, Ans. of Americana). Respondent Americana is a corporation organized under the laws of the State of Delaware (Complaint, ¶ One; ¶ 2, Ans. of Americana). Its principal office and place of business was at 575 Lexington Ave., New York, New York. Until 1972, Americana sold encyclopedias and other publications, merchandise, and services to the general public through various methods, including door-to-door canvassing (Complaint, ¶ One; ¶ 2, Ans. of Americana). After 1972, Americana ceased all business operations (RX 549). Its volume of business has been substantial (¶ 2, Ans. of Americana).

8. Respondent Spencer International Press, Inc. (Spencer) is a wholly-owned corporate subsidiary of respondent Grolier, Inc. (Complaint, ¶ One; ¶ 2, Ans. of Spencer). Respondent Spencer is organized under the laws of the State of Delaware (Complaint, ¶ One; ¶ 2, Ans. of Spencer). Its principal office and place of business was at 575 Lexington Ave., New York, New York. Until 1972, Spencer sold encyclopedias and other publications, merchandise, and services to the general public through various methods, including door-to-door canvassing [7] (Complaint, ¶ One; ¶ 2, Ans. of Spencer; Tr. 15233). After 1972, Spencer ceased all business operations (RX 549). Its volume of business has been substantial (¶ 2, Ans. of Spencer).

9. Respondent The Grolier Society, Inc. (Grolier Society) is a wholly-owned corporate subsidiary of respondent Grolier, Inc. (Complaint, ¶ One; ¶ 2, Ans. of Grolier Society). Respondent Grolier Society is organized under the laws of the State of Delaware (Complaint, ¶ One; ¶ 2, Ans. of Grolier Society). Its principal office and place of business was at 575 Lexington Ave., New York, New York. Until 1972, Grolier Society sold encyclopedias and other publications, merchandise, and services to the general public

through various methods, including door-to-door canvassing (Complaint, ¶ One; ¶ 2, Ans. of Grolier Society). After 1972, Grolier Society ceased all business operations (RX 549). Its volume of business has been substantial (¶ 2, Ans. of Grolier Society).

10. Respondent R. H. Hinkley Company (Hinkley) is a wholly-owned corporate subsidiary of respondent Grolier, Inc. (Complaint, ¶ One; ¶ 2, Ans. of Hinkley). Respondent Hinkley is organized under the laws of the State of Maine (Complaint, ¶ One; ¶ 2, Ans. of Hinkley). Its principal office and place of business was at 575 Lexington Ave., New York, New York. Until 1972, Hinkley sold encyclopedias and other publications, merchandise, and services to the general public through various methods, including door-to-door canvassing (Complaint, ¶ One; ¶ 2, Ans. of Hinkley). After 1972, Hinkley ceased all business operations (RX 549). Its volume of business has been substantial (¶ 2, Ans. of Hinkley).

11. Respondent Grolier New Era Corporation (Grolier New Era) is a wholly-owned corporate subsidiary of respondent Grolier, Inc. (Complaint, ¶ One; ¶ 2, Ans. of Grolier New Era). Respondent Grolier New Era is organized under the laws of the State of Illinois (Complaint, ¶ One; ¶ 2, Ans. of Grolier New Era). Its principal office and place of business was at 575 Lexington Ave., New York, New York. Until some time prior to January 1, 1971, Grolier New Era sold encyclopedias and other publications, merchandise, and services to the general public through various methods, including door-to-door canvassing (Complaint, ¶ One; Tr. 15234). While in business, Grolier New Era did business only in the northeast area of the United States (Tr. 5884-85). Prior to January 1, 1971, Grolier [8] New Era had ceased all business operations (Tr. 15233-34). Its volume of business has been substantial (¶ 2, Ans. of Grolier New Era).

12. Respondent The Richards Company, Inc. (Richards) is a wholly-owned corporate subsidiary of respondent Grolier, Inc. (Complaint, ¶ One; ¶ 2, Ans. of Richards). Respondent Richards is organized under the laws of the State of Delaware (Complaint, ¶ One; ¶ 2, Ans. of Richards). Its principal office and place of business was at 635 Madison Ave., New York, New York. Until June 1972, Richards sold encyclopedias and other publications, merchandise, and services to the general public through various methods, including door-to-door canvassing (Complaint, ¶ One; ¶ 2, Ans. of Richards; Tr. 15998-99). Richards ceased direct sales in June 1972, with the exception of sales from the Dallas office, which ceased in August 1972 (Tr. 15998-99). Its volume of business has been substantial (¶ 2, Ans. of Richards).

13. Respondent Madison Enterprises, Inc. (Madison) is a wholly-

owned corporate subsidiary of respondent Grolier, Inc. (Complaint, ¶ One; ¶ 2, Ans. of Madison). Respondent Madison is organized under the laws of the State of California (Complaint, ¶ One; ¶ 2, Ans. of Madison). Its principal office and place of business was at 635 Madison Ave., New York, New York. From May 1969 to December 1970, Madison engaged in direct sales of encyclopedias and other publications, merchandise and services to the general public, primarily within the State of California (Complaint, ¶ One; ¶ 2, Ans. of Madison; Tr. 5820, 6464). Madison ceased selling by the beginning of 1971 (Tr. 6464). Its volume of business has been substantial (¶ 2, Ans. of Madison).

14. Respondent Grolier Interstate, Inc. (Grolier Interstate) is a wholly-owned corporate subsidiary of respondent Grolier, Inc. (Complaint, ¶ One; ¶ 2, Ans. of Grolier Interstate). Respondent Grolier Interstate is a corporation, organized, existing and doing business under the laws of the State of Delaware (Complaint, ¶ One; ¶ 2, Ans. of Grolier Interstate). Its principal office and place of business is at 575 Lexington Ave., New York, New York. Grolier Interstate sells encyclopedias and other publications, merchandise, and services to the general public through various methods, including door-to-door canvassing (Complaint, ¶ One; ¶ 2, Ans. of Grolier Interstate). Grolier Interstate is the sole [9] domestic subsidiary of Grolier, Inc. presently engaged in direct sales (Tr. 16211-12). Its volume of business has been, and is, substantial (¶ 2, Ans. of Grolier Interstate).

15. Respondent Federated Credit Corporation (Federated Credit) is a wholly-owned corporate subsidiary of respondent Grolier, Inc. (Complaint, ¶ One; ¶ 2, Ans. of Federated Credit). Respondent Federated Credit is organized under the laws of the State of Delaware (Complaint, ¶ One; ¶ 2, Ans. of Federated Credit). Its principal office and place of business was at 575 Lexington Ave., New York, New York. Until early 1973, Federated Credit collected and induced payments on accounts for subsidiary corporations of Grolier, Inc. (Complaint, ¶ One; ¶ 2, Ans. of Federated Credit; Tr. 14726). At various times, Federated Credit has operated as a financing company for companies other than subsidiaries of Grolier, Inc. (Tr. 6436). In early 1973, Grolier Interstate assumed the previous functions and operations of Federated Credit (Tr. 14726). Its volume of business has been, and is, substantial (¶ 2, Ans. of Federated Credit).

16. The record shows that respondents' direct selling or subscription book subsidiaries had the following sales volume in the period 1968 to 1972:

	1968	*1969*	*1970*	*1971*	*1972*
GROLIER SOCIETY, INC.	11,636,459	11,946,044	10,417,301	6,324,311	(1,250,418)
AMERICANA CORPORATION	14,538,083	16,348,360	16,192,541	14,277,336	459,525
R. H. HINKLEY COMPANY	5,886,812	7,178,210	8,030,933	5,007,165	(838,635)
THE RICHARDS COMPANY	17,621,778	17,112,754	13,384,215	10,378,015	4,925,591
SPENCER INTERNATIONAL PRESS, INC.	12,550,945	12,794,249	10,527,857	4,923,672	(816,882)
GROLIER NEW ERA CORP.	213,437	238,292	13,662	(1307)	—
GROLIER INTERSTATE, INC.	—	4,371,704	4,075,449	4,892,462	29,921,994
MADISON ENTERPRISES, INC.	—	57,633	715,796	40,629	(16,965)

(Respondents' Proposed Finding IV 10).

[10] 17. In terms of dollar volume, the record shows that certain of the respondent mail order subsidiaries had the following approximate gross sales for the periods indicated:

	Americana Institute	*Career Institute*	*Grolier Enterprises, Inc.*
1969	$20 million	$1 1/2 million	$20 million
1970	$22 million	$2 million	$25 million
1971	$27 million	$2 1/4 million	
1972	$30 million	$4 million	$29 million
1973	$27 million	$5 million	$34 million

(Green 1707-09)

18. In the course and conduct of their business, as aforesaid, respondents now cause, and for some time past have caused, said publications, merchandise or services to be shipped and distributed from their places of business or from their sources of supply to purchasers and prospective purchasers thereof located in various States of the United States other than the state of origination, distribution or storage of said publications, merchandise or services. Respondents transmit and receive, and cause to be transmitted and received, invoices, checks, collection notices and various other

commercial papers or documents in the course of advertising, selling, or otherwise distributing and collecting payment for said publications, merchandise or services among and between the several States of the United States. Respondents maintain, and at all times have maintained, a substantial course of trade in such publications, merchandise or services in commerce, as "commerce" is defined in the Federal Trade Commission Act (Ans. to Complaint submitted by respondents; CX 5, 8). [11]

II. THE PARENT COMPANY AND ITS SUBSIDIARIES

A. *Organization*

19. In mid-1960, Grolier, Inc., as parent company, assumed publishing and financing functions for a number of respondents' subsidiaries, both in the United States and abroad (Murphy 5709).

20. Respondents operate their business through their subscription book subsidiaries and mail order subsidiaries. The subscription book subsidiaries[1] are engaged in the sale of encyclopedias, and other reference works and services by the door-to-door, installment sales method. The Domestic Mail Order Subsidiaries are engaged in the sale of publications and merchandise through mail solicitations and have no retail sales except through mail presentations (McKean 6405). The stock of the mail order and home subscription companies, prior and subsequent to the 1971 reorganization, was owned by Grolier, Inc. (Murphy 5708, Veras 6190).

21. There has been an extensive overlap in the positions of the officers and directors of Grolier, Inc. and its subsidiaries (McCabe Deposition 13-20; CX 5A-5E, 6A-7S). This is demonstrated by the following tables showing the positions held by certain key officials in the parent company and its subsidiaries as of April 21, 1970:

W. J. Murphy

Director, President, Grolier, Inc.
Director, Americana
Director, Americana Interstate
Director, Chairman of the Board, Federated Credit
Director, Grolier Enterprises
Director, President, Grolier Interstate
Director, Hinkley
Director, Chairman of the Board of Directors, Spencer
Director, Grolier Society [12]

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[1] The term "subscription" is historical. Originally, many publications were sold in advance of their publication date to customers who would subscribe to the publication when completed. Now the term refers to Reference Book sales on a door-to-door, installment basis (McKean 6393-94).

G. W. McKean

Director, Vice President and General Counsel, Grolier, Inc.
Secretary, Americana
Director, Secretary, American Peoples Press
Director, Career Institute
Director, Grolier Enterprises
Secretary, Grolier Interstate
Director, Secretary, Grolier Reading Programs
Director, Secretary, Grolier Society

H. G. Veras

Vice President, Director of Accounting, Grolier, Inc.
Treasurer, Secretary, Director, Federated Credit
Director, Treasurer, Grolier Interstate
Director, Vice President, Treasurer, Grolier New Era
Director, Hinkley
Director, Spencer

S. S. Ball

Director, Treasurer, Grolier, Inc.
Treasurer, Americana
Director, Americana Interstate
Director, Career Institute
Treasurer, Richards

E. S. Howell

Director, Vice President, Grolier, Inc.
Director, Secretary, Americana Interstate
Director, Secretary, Career Institute
Director, Grolier Enterprises
Director, Grolier Reading Programs

(CX 5A-E, 6A-S)

22. The parent company, Grolier, Inc., directs and controls the financial policy, the overall sales policies, and administrative and personnel policies of its subscription and mail order subsidiaries (CX 5H; Special Report in Response to Federal Trade Commission Order, dated March 13, 1970). Grolier, Inc. exercises control over its subsidiaries in the following manner: [13]

> . . .Grolier directs and controls the overall financial, sales, administrative and personnel policies of each of its subsidiaries through directives, both written and oral, promulgated by the President of Grolier (with respect to the Subscription Book Companies); the Grolier Vice President, Director of Mail Order Divisions (with respect to the Mail Order Division); and the President of Grolier Educational Corporation (with respect to Grolier Educational Corporation). Company matters and policies affecting both Grolier and the subsidiaries are normally submitted by the President of

> the subsidiary to one of the above described officers who, if he deems it appropriate, will submit the matter for the review and direction of the Executive Committee which in turn promulgates directives through such officer. . .In addition, both oral and written communications are promulgated by Grolier's Vice Presidents of Accounting, Personnel Programs, Marketing Services, Customer Relations and Insurance. In general, oral and written directives promulgated by Grolier are relayed to the Presidents of the subsidiaries who are responsible for relaying such directives to the appropriate department heads and branch offices, field offices and sales representatives

(CX 118B-C; see also, CX 5J).

23. Members of the Executive Committee were in charge of the operations of various of the subsidiaries. On April 21, 1970, the Executive Committee of Grolier, Inc. consisted of the following individuals: Fred P. Murphy, Elsworth S. Howell, E. J. McCabe, Jr., Gordon W. McKean, William J. Murphy and F. B. Taussig (CX 5J-K). In addition to being members of the Executive Committee and occupying key positions in Grolier, Inc., most of these individuals occupied top management positions in various subsidiaries of Grolier, Inc. (Finding 21, *supra;* CX 5b-e, 6a-s). The Executive Committee generally met at least once a month (McCabe Deposition 20). William J. Murphy was in charge of the operations of the domestic home subscription subsidiaries (McCabe Deposition 12-13). Elsworth Howell was charged with the supervision of the mail order subsidiaries until his retirement at the end of 1973. Since that period of time, the mail order companies have been under the jurisdiction of William J. Murphy (McCabe Deposition 21-23). [14]

B. *Parent Company Services and Support for its Subsidiaries*

24. Prior to the 1971 reorganization, Grolier, Inc. provided the following services to its mail order and book subscription subsidiaries, *viz.,* publication of certain of the products, financial assistance, and miscellaneous headquarters functions such as insurance, legal work and general accounting (Murphy 5716-17). Such services performed for the subsidiaries by Grolier, Inc. would be construed as a charge credited to the parent company (Murphy 5718).

25. The Vice President and Controller of Grolier, Inc. is the Chief Accounting Officer for the parent company and all its subsidiaries (Veras 6160). The Grolier, Inc. Accounting Department sets the procedures which the accounting offices in the subsidiaries are required to follow (Tr. 6163-64, 6167). The individual subsidiary companies send monthly reports to Grolier, including balance sheets and profit and loss statements. Such information is consolidated by Grolier, Inc. into the final figures (Tr. 6163).

26. Grolier, Inc. files a consolidated federal income tax return for all of its United States corporations (Veras 6168), and, in some cases, Grolier, Inc. will file a consolidated state and local income tax return for its subsidiaries (Veras 6169–70). The individual sales transactions of the subsidiaries are also ultimately reflected in the parent company's public financial reports (Murphy 5713).

27. The subscription book companies, prior to the formation of Grolier Interstate, received operating funds through the company account between them and the parent company in the form of books that were shipped on their accounts or direct remittances from the treasurer (Murphy 5713).[2] Grolier, Inc. maintains a line of credit with banks; the individual subscription book companies do not (Tr. 5715). The subscription book subsidiaries and the mail order subsidiaries have not obtained their own financing separate and apart from the parent company (Murphy 5716). [15]

28. The profit-sharing or retirement plans in which the subsidiary companies participated emanated from the parent company, Grolier, Inc. (Veras 6192).

In the period 1967–1972, the subsidiaries were charged a management fee by the parent company of 4 percent of sales (Veras 6186).

29. Grolier, Inc.'s Marketing Services Department provides national advertising and sales promotional material for respondents' domestic sales organization, and engages in public relations for Grolier, Inc. (Waller 5785). Grolier, Inc. pays for the advertisements put into national publications. The subsidiaries of Grolier, Inc. selling door-to-door do not run their own national advertising (Waller 5793). The purpose of the coupons in certain of the advertising placed by the Marketing Services Department is to develop leads (Waller 5793–94).[3] Grolier Interstate pays the department for such leads (Waller 5795). The Marketing Services Department also runs institutional ads to explain Grolier's policies (Tr. 5797; CX 1606).

The Marketing Services Department prepares a broad spectrum of sales promotional materials, including contest materials, broadsides, flyers, prospectuses and materials to be handed out at booths. In addition, it prepares recruiting materials such as booklets outlining the company history and benefits (Waller 5797–98). Managers of the sales subsidiaries purchase such materials direct from the warehouse of the Marketing Services Department (Waller 5801).

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[2] *E.g.*, a subsidiary such as Americana would obtain funds to pay commissions to its salesmen either from accounts already being collected, an additional advance from the treasurer of Grolier, Inc. or its own central treasury (Murphy 5715).

[3] For example, in advertisements for the *New Book of Knowledge*, the reader is invited by the coupon to send for a free copy of a booklet, "The Magic Carpet." The names of those responding are sent to the manager of the sales subsidiary in the prospect's area (Waller 5794; CX 1611H).

All sales promotional material is to be cleared through the Director of Marketing Services who, in turn, checks with the parent company's Legal Department (Waller 5802). The majority of the material used in the field is prepared by the Marketing Services Department *(id.)*.[4] [16]

30. The sales representatives of the home subscription subsidiaries rely in their sales presentations to the consumer on the name, reputation and goodwill of the parent company, Grolier, Inc. (*e.g.*, see CX 973A-B, 809A, 439B, 971B, 969A; Johnson 9516; Nesper 9784-86; Kolkhurst 10023; Hanke 10425).

C. *Parent Company Control Over Subsidiary Employment and Recruiting Practices*

31. Grolier, Inc. has exercised its power to control the hiring practices of its subscription book subsidiaries (CX 1910, 1924A-B). In one instance, the subsidiary corporations were forbidden to hire or interview present or former employees of another encyclopedia company without clearance of parent company officials in New York. On another occasion, the transfer of personnel from one subsidiary to another was forbidden unless the individual had been away from the first company for twelve full months. Elaborate procedures to ensure that such directives were followed by the subsidiaries were set up by the parent company (CX 1924).[5] [17]

32. In the period 1967-69, the subscription book subsidiaries sent copies of their recruiting advertising to Grolier, Inc.'s Customer Service or Legal Department (Murphy 16442). The record further shows that in the period 1965-67, a Vice President of the parent company had been responsible for reviewing the recruiting advertisements of the Americana Corporation (Mawle 3483).

In addition, "shoppers" were retained to be hired by subsidiaries to determine the facts with respect to their recruiting practices (Murphy 5726, 16442).

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[4] The subsidiaries have on occasion prepared their own sales materials but they are not supposed to (Waller 5801-02).

[5] By memorandum dated May 5, 1969, the subsidiaries were instructed in pertinent part that:

> "Working papers on all new people must be in the New York Personnel office's hand within a week of their first accepted order.
>
> "There will be no transfer of personnel from one company to another unless the individual has been away from the first company for twelve full calendar months.
>
> "Any person found using a flag, or some relative's name, or different social security or tax numbers will be suspended from the Grolier companies.
>
> "Any transfer must be approved in writing by the President of the releasing subsidiary company and accepted by the President of the receiving subsidiary company."

(CX 1924A.)

33. In compensating salesmen, the subsidiaries must stay within the range prescribed by the parent company (McCabe Deposition 31-32).

D. *Parent Company Control Over and Involvement in the Sales Practices and Operations of Its Subsidiaries*

34. The executive Committee of the parent company decided whether a particular subsidiary should have distribution rights to certain publications (Murphy 5719-20). The prices charged by the respondent subsidiaries for the publications sold by them were approved by the Executive Committee of the parent company. In this connection, the parent and subsidiary attempted to achieve a consensus on such prices (Murphy 5721).

35. In the middle of 1967, Grolier, Inc. began to set up procedures for the Customer Service Department whose purpose it was to apprise headquarters of developing problems (Murphy 5727).[6] In the year 1967, 1968 or 1969, as part of this attempt to ensure conformance with the Assurance of Voluntary Compliance accepted by the Commission in 1967, sales materials and presentations of the subsidiaries were brought to headquarters and reviewed (Murphy 5726). The Customer Service Department, through review of these materials and field research, was to find out what sales persons were [18] actually doing in the field and to take care of customer problems (Tr. 5727). In the period 1969–January 1, 1971, the Customer Service Department also handled relations between Better Business Bureaus and Grolier subsidiaries, as well as contacts with Attorneys General and the Federal Trade Commission on behalf of such subsidiaries (Trachtenberg 5673).

36. Grolier, Inc.'s Director of Customer Relations, Norman Trachtenberg,[7] had overall supervision of the Customer Relations Department of the subsidiaries, including the mail order subsidiaries, Grolier Enterprises and Americana Interstate (Tr. 5667). His immediate supervisor was William J. Murphy, the President of the parent company (Tr. 5668). Mr. Trachtenberg made periodic visits to the field and went out with sales representatives. These activities would be reported to Mr. Murphy (Tr. 5675).

37. To ensure that consumers with problems were taken care of, customers were sent a letter from the subsidiary with the receipt of their order encouraging them to respond to the Customer Service

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[6] ". . .I, as president of Grolier Incorporated, had some people doing some field research, trying to determine whether or not what we were being told was in fact going on." (Tr. 5726).

[7] Mr. Trachtenberg held this position when he testified on June 18, 1974 (Tr. 5665). He is also a Vice President of Grolier Interstate, handling new types of sales operations (Tr. 5669).

Department with complaints Murphy 5727-28). In 1969 or 1970, respondents added a "cool line" urging customers to call the Customer Service Department directly with their problems. The Customer Service Department also had the function of reviewing case histories to determine the nature of sales problems (Murphy 5728).

38. In the period 1967-1969, Grolier, Inc. instituted telephone surveys of sales to monitor the efforts of the Grolier subsidiaries' management to implement parent company policy (Murphy 16438). Memoranda summarizing such surveys were sent to the President of the parent company for his review (Murphy 5728). Such telephone surveys were made of 5 to 10 percent of recorded sales (Murphy 5729). [19]

39. Around November 1970, respondents commenced operation of the telephone verification system (Trachtenberg 5674).[8] Under this procedure, after January 1, 1971, employees in respondents' fiscal offices were to call the consumer, question him concerning his understanding about the contract, and ask questions about the sales presentation within 48 to 72 hours of execution of the contract (Trachtenberg 5676).[9] Such verifications would be supervised and checked by Norman Trachtenberg, Vice President and Director of Customer Relations for Grolier, Inc. (Trachtenberg 5665, 5677).[10]

40. Mr. Trachtenberg, prior to January 1971, had authority to adjust or cancel contracts of all Grolier, Inc.'s door-to-door subsidiaries (Tr. 5675-76). He had the power to cancel contracts without consulting the direct selling subsidiary involved (Trachtenberg 5680).

In addition, if a salesman appeared to be intractable in refusing to follow company sales policies, further orders would not be accepted from him (Murphy 5729-30).[11] [20]

E. *The Grolier Interstate Reorganization*

41. In the fall of 1970, William Murphy, President of Grolier, Inc., "made a trip around the country and found that problems were just

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[8] After January 1, 1971, the function of the Customer Relations Department changed only insofar as the new verification procedure was implemented (Trachtenberg 5676).

[9] In this time period, the fiscal offices in question belonged to Grolier Interstate; at times, such calls might also be made by an office of Federated Credit (Trachtenberg 5677).

[10] "A. Well, as I told you before, we take these verifications with the customers' permission and with an approved beep connector, we sample 10% of the tapes around the country, send them into New York and listen to them, to make sure the verification is being done properly.

"And, my staff makes periodical visits around the country and listens to the actual tapes being made" (Trachtenberg 5678).

[11] An Americana office in Minnesota and a Spencer Press office in St. Louis were closed down prior to 1971 for similar reasons (Murphy 5731). A Richards' office in the Philadelphia area was closed down because of difficulties with the Better Business Bureau in that city (Murphy 5733-34).

as rampant" (Murphy 5735). In late November or early December 1970, key management people were informed that door-to-door sales operations were to be put together under one roof as Grolier Interstate so as to effectuate supervision and control by the first of 1971 (Murphy 5736). Grolier Interstate officially came into being in 1971 (Tr. 5737–38) becoming the one subscription book subsidiary of Grolier, Inc. for the entire United States in January of that year (Murphy 16396).[12] Grolier Interstate was created because Grolier, Inc. was unable to secure the five door-to-door sales subsidiaries' compliance in the field with the sales practices and procedures established by the parent company (Murphy 5734). Over a two to three-year period, the management of the parent corporation had become persuaded that it would not be possible to get the domestic selling organizations under control in the face of four to five separate sales subsidiaries competing with each other (Murphy 5735).

42. Under the reorganization, eight regional managers were to take all responsibility for all home field subscriptions in their territory and it was their duty to integrate the formerly separate organizations of Grolier, Inc.'s subsidiaries into one business enterprise (Murphy 5740). The former subscription book subsidiaries such as Americana still exist as legal entities but they do not function operationally (Murphy 5741, 16435). It was decided not to include Richards in the Grolier Interstate reorganization because of the differences in its operation methods as compared to other subsidiaries and because "we had had—by that time too many complaints and too many sales problems" (Murphy 5736, 5749, 16405–06).[13] [21]

43. The parent company Grolier, Inc. ran an institutional advertisement in its name on October 28, 1971, in some 43 newspapers (CX 1606; Waller 5796). The advertisement was entitled "After you've said yes to our salesmen you can still say no to the company:" In pertinent part, the advertisement stated:

> After our salesman has left your home, you can still change your mind about the encyclopedia you've bought. No matter what you've signed, no matter what you've said. And no matter what you may have heard to the contrary.
>
> * * * * * * *
>
> Yet we know that doubts and second thoughts sometimes arise. So we have instituted a consumer protection program which not only provides many means by

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[12] A pilot program of this nature under the Grolier Interstate name had previously been conducted in the Pacific Northwest commencing in 1968 (Murphy 16393–94, 16398).

[13] According to Grolier, Inc.'s chief officer "the Richards' sales practices were causing as much of our problems as — or more than some of the others, and I wasn't sure that we could go through the lengthy period of time of reorganizing and retraining this group of people." (Murphy 16406).

which the customer can communicate directly with the company, but guards him against dissatisfaction and misunderstanding.

The "Cool Line"

Grolier's "Cool Line," a special telephone number printed on the contract, allows a customer to call collect our Vice President of Customer Service in New York. It provides direct access to someone with authority to solve a problem, whatever it might be.

Cancellation Privileges

Our standard sales contract stipulates a "cooling-off" period and states how a customer can cancel an order. The contract also states that this is not a special offer; that there are no items that are free. It discloses all terms, including finance charges, so there is no confusion as to what the customer is buying or how he is paying for it. It lists prices so the customer won't be misled. [22]

Double-Check Phone Call

When an order is received, but before it's accepted, every customer receives a phone call from someone in no way connected with our sales department. We discuss the entire transaction with the customer to find out if there has been any misunderstanding or misrepresentation. That way, the customer is given every opportunity to reveal any dissatisfaction either with the product or method of sale. If there is any misunderstanding and it is not cleared up to the customer's complete satisfaction, we'll cancel the order and return the down-payment.

When an order is accepted, we write and thank our customer. Enclosed with this letter is a copy of the contract, an envelope addressed to the company president inviting comments, and the "Cool Line" phone number should he wish to call.

Call From Headquarters

Eight weeks after the order has been shipped, we telephone from New York to a random ten percent of our customers to make a broad sampling of their reactions to our publications, our sales personnel—particularly their conduct and presentations—and to make sure that the company's customer protection policies have been thoroughly carried out.

Admittedly, we've had problems. We've discovered most of them ourselves, and where necessary, dismissed personnel . . . and closed sales offices.

Customer Satisfaction Guaranteed

What all this means is that we at Grolier have a particular way of thinking about our customers: we value their trust and goodwill. [23]

Someday a Grolier salesman may call on your family. We hope you'll feel confident about welcoming him into your home. And that would be good for us both.

GROLIER INCORPORATED

575 Lexington Ave., New York, N.Y. 10022

44. Through the foregoing, the parent company has represented to the consuming public that it is responsible for the actions of the

salesmen of its direct selling subsidiary; that it has taken the necessary steps to prevent consumer deception and if necessary to ameliorate its effects. The advertisement further represents to the public that the parent company has the power to dismiss personnel and close sales offices to assure consumer protection. Through such representations, Grolier, Inc. invites the public to place its confidence in the salesmen selling Grolier products in reliance on the parent company name. This advertisement demonstrates that the parent-subsidiary operation is inter-related, constituting one enterprise. The use of terms such as "our salesman," "our standard sales contract" and "our customer" represents that the parent-subsidiary distinction has no meaning as far as the consumer is concerned.

45. Divisions of Grolier Interstate, after the reorganization, still used contracts bearing the names of certain of the subsidiaries in those areas where they had prior sales strength (Murphy 5743). At the time of Grolier Interstate's creation, the former door-to-door sales subsidiaries were designated as divisions of Grolier Interstate (Murphy 5741). These division offices, since the 1971 reorganization, have been organized by the products sold (McKean 6469).

46. After the formation of Grolier Interstate and after January 1, 1971, Federated Credit offices still handled accounts as part of the Grolier Interstate organization (Murphy 5746–48).

47. Subsequent to the reorganization, retail sales [24] contracts passed through[14] the Grolier, Inc. headquarters' legal offices for approval (Murphy 5742, 5764).

When a new sales presentation is formulated by a district manager, it is reviewed by the Legal Department of Grolier, Inc.[15] and sales presentation materials are developed by the Marketing Services Department headed by Irene Waller (Trachtenberg 5670–71). Grolier, Inc. had final okay on sales presentations used by all of its sales organizations (Trachtenberg 5679).

48. After the formation of Grolier Interstate, William J. Murphy, as President of Grolier Interstate,[16] reviewed recruiting ads obtained from the field and established policy relating to the content of such advertisements, which were disseminated to the various managers of Grolier Interstate. In the same capacity, Mr. Murphy also reviewed sales presentations which had been brought to his attention (Murphy 5745).

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[14] Grolier Society, Spencer and Americana were the primary names carried forward and, as of 1974, there were Grolier Society and Spencer divisions (Murphy 5743). No one, however, has worked as a Hinkley representative since the summer of 1971 *(id.)*.

[15] Testimony pertains to period after formation of Grolier Interstate.

[16] Mr. Murphy, at the same time, was chief officer of the parent company, having held this position since 1967 (Murphy 5709).

49. Mr. Murphy, in January and August 1971, sent directives to regional managers of Grolier Interstate to assure uniform pricing of the combinations of encyclopedias and other products sold (Murphy 5760-63; CX 1870A-B, 1871A-B).

F. *Parent Company Knowledge of Subsidiary Sales Practices Occurring in the Field and Difficulties Experienced in Controlling Field Management*

50. The parent company had and still has the power to control the recruiting and sales practices of its subsidiaries (Findings 19-49). And it has exercised that power. Such [25] power has, however, not been always effectively exercised to prevent misrepresentation (See *infra*). The history of respondents' business has been such that field management has not been responsive to directives from the head office. "A system of management evolved where each local, regional or branch manager took total control of his operation and on many occasions just refused to obey any kind of a directive from New York" (Toman 16233-34,[17] 16237-39).

51. Nor did respondents achieve satisfactory control of the sales organization at the time of the Grolier Interstate reorganization in January 1971 because "the machinery to exercise the control was not set up at the proper time" (Toman 16234) and "while Grolier was put together on paper in the beginning of 1971, it was far from reorganized" (Toman 16235).

The actual buildup of the headquarters staff deemed necessary to achieve control over the sales organization in the field commenced in 1973, when John Toman succeeded William Murphy as President of Grolier Interstate (Toman 16239-41).

52. The officials of the parent company, Grolier, Inc., through the telephone survey, were aware that the respondent book subscription subsidiaries were engaging in the types of misrepresentation challenged by the complaint. As a result of such surveys, executives of the parent company were aware in 1969 that the subscription book subsidiaries had misrepresented that salesmen are conducting a survey; that books are free; that customers are just paying for the research service; [26] that books are not yet on the market; that the prospective customer had been specially selected; that the customers'

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[17] *E.g.*, see the response by one of respondents' executives:

". . .The organization was not being controlled by New York because it was not responsive to New York, and it was very difficult for New York to exercise any control because you had four separate corporations with four separate Presidents with probably eight or nine branch vice presidents in each of the operations; and this heirarchy had developed and it became impossible to control — to exercise control over the operations because if corporate management would say, 'Let's lean on Americana Corporation,' the people from Americana would go over and work for Grolier society and they were getting — they were almost like sharks eating each other up. It was an impossible situation to control." (Tr. 16234.)

home was to be used as a showcase; and the amount of savings available if the offers were accepted (*e.g.*, CX 110, 113, 77A-D, 79A-D, 82A-Q, 85A-K, 90A-J, 96A-J, 97A-J, 106A-K).

53. The executives of Grolier, Inc., moreover, were aware that the incidence of such misrepresentations by the direct selling subsidiaries were substantial. Consider, for example, the report to the parent company's chief executive, dated October 29, 1969, for the week ending October 25, 1969, stating as follows:

> During the above week, we checked 198 orders and completed interviews with 158 customers. We came up with a 17% violation rate.
>
> In the special summary sheet enclosed, you will find that our special problem areas are Chicago, which is now really St. Louis, Houston and Los Angeles showing 22%, 20% and 18% respectively.
>
> If I ran the same check a week later it might be much higher. However, I think that those three areas are the areas we must concentrate on.
>
> This special survey idea enables us to get a larger sampling and verify the results of the standard weekly survey for all subsidiaries. With your approval, I will continue it on a spot basis. [27]
>
> The violations that we are uncovering are still selectivity, price buildup and free merchandise.

(CX 110F.)[18]

54. Grolier, Inc.'s problems, generated by its inability to make its subsidiaries conform in the field to the parent company's announced practices and policies, were still evident in 1970 (Murphy 5734-35). These problems persisted, even after the Grolier Interstate reorganization. Field management officials on the vice presidential level were being dismissed for failing to prevent consumer misrepresentations as late as 1973-1974 (Toman 16357-60). [28]

III. RECRUITMENT OF SALES PERSONNEL[19]

A. *Advertisements*

(1) Dissemination of Advertisements

55. In the regular course and conduct of their business and for the purpose of recruiting personnel for solicitation of door-to-door sales, local offices of respondents have disseminated, and have caused to be disseminated, advertisements in various publications of general circulation (Mawle 3452, 3456, 14786; Kotler 5059-60;

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[18] The report dated November 5, 1969, disclosed an "alarming 35% violation rate." A total of 63 violations was found for 237 orders contacted of which 197 were checked for the week ending November 1, 1969 (CX 111C).

On December 18, 1969, a violation rate of 13 percent was reported, which was described as "now down to where it belongs" (CX 116C).

[19] Throughout this section, the term "respondents" refers to the parent company and those respondents identified in Section I, *supra*, as having engaged in subscription book sales.

McClearey 13826–27, 13831; Goldstein 14123; Stearns 14603; Basilici 14926–27; Toman 16300). These publications include the *Oakland Tribune, Boston Globe, Denver Post, Orange County Reporter, Buffalo Evening News, Rockey Mt. News, Daily Oklahoman, Milwaukee Journal, Seattle Times, Peoria Journal Star, Kansas City Star, Des Moines Register* and *Los Angeles Times* (Havas 9199; Tepker 9436; Johnson 9511; O'Hara 9978; Kellogg 10925; Russell 10375; Thorn 11158; Walker 11213; McNamara 11270; McWilliams 11994; Miller 12791; Howard 12892; Hanna 13189; McClearey 13826; Loots 14668).

56. No single type of recruitment advertisement was used by the respondents; ads placed by the respondents would vary considerably in content (Covens 13645, 13653). Recruitment advertisements used by respondents' local offices were reviewed by the various subsidiaries of respondent Grolier, Inc. or approved for use prior to publication by respondent Grolier, Inc., which disseminated to the local offices a manual containing such approved advertisements (Stearns 2613–15, 14603; Mawle 3452, 14786; Covens 13645; McClearey 13827, 13974–75, 13997).

57. Respondents placed recruitment advertisements in various columns of the classified sections of newspapers, including "Direct Sales" or "Sales Help Wanted" (CX 2085, 2100B); "Help Wanted" (CX 1033, 1557, 1649Z–7, 1650F, 1696B, 2096D, 2104B, 2107B); "Employment" (CX 1677C); "Jobs of [29] Interest" (CX 1669B, 1674C); and "Miscellaneous" (CX 2103B). Placement in columns not designated "Sales" was sometimes necessitated by the lack of such column in a given newspaper (Havas 9199). In other instances, although a "Sales Help Wanted" column existed, recruitment advertisements were placed in other columns (CX 1557, 1650F). In addition to column designations, recruitment advertisements sometimes had job designations such as "sales", "Educ. Sales," "MGMT." or "INTERVIEWERS" in the upper corner of the ad (CX 1669B, 1674C, 1696B, 1703A).

(2) Blind Advertisements

58. In seeking to attract applicants for sales work, respondents placed various "blind" recruitment advertisements which did not disclose the nature of the position offered, the company name, or the product involved (CX 1557, 1568A–B, 1569, 1573, 1574, 1649Z–7, 1650F, 1669B, 1698B, 1701C, 1703B, 1704B, 2085; Mawle 3453, 14786; Kotler 5065; Vaughn 5879–80; Will 9596; Gilbow 12192, 12195, 12201–03, 12408; McClearey 13975; Goldstein 14076, 14124; Basilici 14927).

59. The following "blind" recruitment advertisements are illustrative of those placed by respondents:

$115 WK. SALARY

Young women (18-25) now being hired for interesting work with local office of world wide company. No previous exp. required as full on the job training will be given. Excellent advancement opportunities & unrivaled security. Applicants must be able to start immediately, should telephone 258-3319 between 9:30 a.m. & 2:30 p.m. for interview appointment.

(CX 22E)

INSTRUCTORS NEEDED

WILL be trained for stimulating work in field of linear programm-[sic] ming, good speaking voice and appearance req. high school and college graduates pref. First year expected earnings $8000-$15,000, no experience nec., car req. For interview call MR. DAVIDSON between 12-2 p.m. 893-7140

(CX 779) [30]

Female

BUSINESS OPPTY!!

Have 5 immediate openings for right person - single, under 25. No experience necessary, will train and salary in field of sales administration and personnel. $450 beginning salary in our book order dept. with our rapid growing firm. Before 2 p.m. EX 2-2123

(CX 1033)

SALES

COLLEGE STUDENTS—EVERY STUDENT WILL RECEIVE ONE SCHOLARSHIP

YES. EVERY STUDENT THAT WE EMPLOY BEFORE JULY 17th WILL RECEIVE A CASH SCHOLARSHIP IN ADDITION TO REGULAR EARNINGS, PROVIDING THEY REMAIN IN OUR EMPLOY FULL TIME FOR THE ENTIRE SUMMER.

Students will do promotional interview work in our educational tool department.

NO EXPERIENCE NECESSARY. OPENINGS LOCALLY AND IN SOME RESORT AREAS.

Guaranteed Salary $500 per mo.
Call our nearest branch office:
Hayward office 582-2414

* * * * * * *

(CX 1677C.) [31]

MGMT.

Opportunity for Men and Women Local division of international firm will hire 10 people to work in promotion department. No previous experience. Company handles

all training. Earning in excess of $550 month, bonus and incentives. Must be high school graduate, neat in appearance, converse intelligently. Rapid advancement available. Start work immediately. For interview appt. call 623-0720

(CX 1696B).

(See also CX 20, 22A, 1557, 1649Z-7, 1650F, 1669B, 1674C, 2096C, 2100B, 2104B.)

60. Frequently, blind recruitment advertisements used by respondents affirmatively misrepresented that the positions offered were non-selling in nature. The employment offered was characterized as: public relations work (Thorn 11158), including marketing and promotions (CX 22C, 2110B, 2111B, 2112B; Havas 9199); conducting interviews (CX 22D, 1674C, 1677C, 2096D, 2108B; Howard 12892; Loots 14668) and opinion poll surveys (Miller 10167; Kellogg 10295); "instructors" in linear programming (CX 779; Hanna 13189-90); inventory work (Tepker 9436); advertising work (Williams 9938; Hanke 10416); sales administration and personnel (CX 1033); and management (CX 22D).

61. Due to the high turnover rate of sales employees, respondents continually concentrated on recruiting new sales personnel (McClearey 13898, 14018; Basilici 14946, 14949). Use of blind recruitment advertisements were successful in eliciting a large response by applicants (Gilbow 12408, 12410; McClearey 13975) and were, therefore, the major, if not exclusive, recruiting tool used by respondents.

62. Respondents' corporate officials and management agree that an accurate description in recruitment advertisements of the position offered would result in few, if any, applicants (Covens 13658; McClearey 13836; Goldstein 14125-26; Stearns 14606-07; Mawle 14789; DeLucia 15057-58; Ryan 15928; Toman 16300-03). If recruitment advertisements disclosed that door-to-door encyclopedia sales positions were offered, "nobody [32] would answer such an ad" (Ryan 15928) because "[n]ot too many people want to be door to door salesmen" (DeLucia 15058).

63. When interested persons called the phone numbers given in respondents' recruitment advertisements, an interview was set up, but even if requested, they were given no additional information as to the nature of the employment offered (Snyder 8718; Havas 9200; Will 9596; O'Hara 9979; Kolkhurst 10017; Kellogg 10296; Hanke 10417; Evans 10608; Thorn 11159; Walker 11214, 11231; Davenport 11704-05; Latasa 11801-02; McWilliams 11995, 12023; Miller 12824-25; Hanna 13189). It was respondents' policy not to disclose on the

phone exactly what the job involved (Kotler 5064-65; DeLucia 15058-59; Toman 16303; Murphy 16419-20).

64. Numerous applicants who responded to blind recruitment advertisements placed by respondents would not have done so had they been informed by the recruitment advertisements or during the phone call setting up an interview that the positions offered were in the field of door-to-door sales of encyclopedias and other educational materials (Havas 9200; Kellogg 10295; Waugh 10497; Walker 11214; Westheimer 11437, 11471; Davenport 11745; Nelson 12671; Miller 12792; Gribbin 13119; Goldstein 14125).

(3) Advertisements Offering "Management Training"

65. Respondents also placed advertisements in local papers which offered employment opportunities for "management trainees" (Mawle 3455; Kotler 5063; Westheimer 11466; Gilbow 12202-03; Covens 13658, 13735, 13750; Stearns 14605; DeLucia 15054). Representations contained in such advertisements imply that formal management programs are offered and that advancement within the organization is dependent upon the successful completion of such programs. These recruitment advertisements did not disclose the company or products involved or that door-to-door sales were inherent in the positions offered (CX 1570, 1571, 1572, 1696C, 1698B).

66. The following "management trainee" advertisement is illustrative of those placed by respondents:

APPRENTICES — HIGH SCHOOL GRADS
Recently discharged vets [33]

18-25
No Experience Necessary
$141 SAL. PER WEEK

Work where your age is an asset, not a liability. International corporation hiring 5 men for a management training program in our book sales dept. For personal interview call: Mr. Rudd, 362-7213

(CX 22D).

67. Applicants responding to "management trainee" advertisements were, in fact, hired to work as door-to-door salesmen and received training which was identical to that given applicants who responded to non-management recruitment advertisements (Mawle 3455-56; Johnson 9526; Miller 12799; DeLucia 15054, 15083; Toman 16322-23). As is evidenced by the following testimony, respondents

had no formalized management training program at the time management trainee advertisements were disseminated:[20]

> Q. Mr. Gilbau, during the time that you were associated with Americana Corporation and on the occasions that you used a recruiting advertising that contained the phrase management training to recruit sales personnel, did you ever have a formal management training program in existence?
>
> A. No.
>
> Q. Did you have any management training program in existence?
>
> A. Well, per se, no.

(Gilbow 12205.)

> [34] Q. What type of management training program was set up by Spencer in Los Angeles?
>
> A. After a person got in the sales production and showed that he could sell, that he knew the presentation and showed an aptitude for the business, we would give him his first responsibility which would be a crew manager . . ." (Kotler 5063)[21]

* * * * * * *

> Q. Was the training of people who responded to that advertisement [not referring to management training] any different from the training for the people who responded to the management training ad?
>
> A. No.

(*Id.* at 5064.)

Advancement from sales into management was based on a demonstrated ability to sell rather than the fact that an applicant had responded to a management training advertisement (Covens 13661-62, 13738; DeLucia 15057).

(4) Compensation Guarantees in Recruitment Advertisements

68. Recruitment advertisements placed by respondents frequently contained compensation guarantees for the positions offered (Stearns 2616, 14625; Mawle 3452; Kotler 5060; Vaughn 5880; Covens 13647, 13723-24; McClearey 13931; Basilici 14928). These compensation guarantees were usually expressed in terms of an hourly (*e.g.*, $3.00/hr.), weekly (*e.g.*, $145/wk.) or monthly (*e.g.*, $550/mo.) salary (CX 20, 22A, D, E, 967, 1033, 1564, 1565, 1567, 1569, 1570, 1571, 1572,

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[20] There is some testimony in the record that various types of informal management training occurred at different times at the regional or local levels (Covens 13662; McClearey 13977, 13997-98, 14010-11; Stearns 14626-27; Toman 16306, 16322). The record also shows that certain of respondents' local offices utilized management training recruitment advertisements at times when no management training program was being offered at such offices (Gilbow 12205; Kotler 5063-64; Miller 12799; Johnson 9526; Westheimer 11466-67).

[21] Formalized management training for new recruits appears to be a relatively recent development (see Toman 16322).

1573, 1574, 1577, 1649Z-7, 1650F, 1677C, 1696B, 2085, 2096D). In other recruitment advertisements, representations of potential or average yearly earnings (*e.g.*, $10-12,000) for the position offered were made (CX 21, 779). [35]

69. Offering salary or compensation guarantees was an excellent tool for recruiting sales personnel (McClearey 13934-35). Respondents' rationale for making guarantees was that they ostensibly assured income security to applicants and provided a mechanism for controlling training of new employees since the job performance of individuals seeking to obtain the guarantees were more closely scrutinized (McClearey 13934-35; Basilici 14930-31).

70. Conditions which were later placed on obtaining the offered "guarantees" were either entirely absent in recruitment advertisements (CX 779, 967, 1033, 1557, 1574, 1649Z-7, 1650F, 1677C, 1696B, 2085, 2096B) or were impliedly made by an "if qualified" addendum appearing in the advertisements without any explanation or amplification as to the nature of such qualifications (CX 20, 22A, 1564, 1565, 1567, 1569, 1570, 1571, 1572, 1573, 1674C). Respondents' officials confirmed that it was respondents' policy not to disclose in their recruitment advertisements the conditions which applicants would be required to meet in order to receive the offered guarantees (Stearns 2617-18; Covens 13725-26; McClearey 13931; Mawle 14788; Ryan 16050).

71. The income guarantees made in respondents' recruitment advertisements were a critical factor in some individuals' decisions to apply for the positions offered (Walker 11230-31; Davenport 11704; Latasa 11799; Nelson 12671; Miller 12792; Culver 12940; Gribbin 13148).

72. Neither the recruitment advertisements placed by respondents nor information given over the telephone when interested individuals called in response to such advertisements disclosed that:

(1) the positions offered were for door-to-door salesmen;

(2) no formal management training program existed nor would applicants responding to management training advertisements necessarily receive an opportunity to advance into management;

(3) conditions were placed upon receipt of the guaranteed income or salaries mentioned in recruitment advertisements. [36]

The fact that the position offered involved door-to-door sales; that management training was not readily available; and that conditions were placed on receipt of the guaranteed salaries or income were all material facts which would have an effect on a prospective employee's decision to respond to respondents' recruitment advertisements. Failure to disclose these material facts was, therefore, false, misleading and deceptive.

B. *Disclosures Made during Initial Interviews and Training*

(1) Characterization of Employment

73. During their initial interviews, prospective employees responding to blind recruitment advertisements were given varying descriptions of the employment offered. Respondents' official disclosure policy was to give a full and accurate description of the jobs offered during an applicants' initial interview (Toman 16303-04; Murphy 16419-20; see also McClearey 13837-38; Mawle 14788; DeLucia 15058-59; Ryan 15929). In accord with this policy, some applicants were informed during their initial interview that the job offered involved encyclopedia sales (Snyder 8719, 8772; Johnson 9512; Gilbow 12119; Miller 12821-22). Other applicants ascertained that selling would be involved during their initial interviews although the products to be sold were not fully identified, and they were not explicitly told that selling would be involved (Havas 9203; Waugh 10498-99; Westheimer 11499; Hanna 13200-01).

74. Despite the official policy of full disclosure, many applicants were not aware at the conclusion of their initial interviews that the employment offered by respondents encompassed sales. The employment descriptions given these applicants reiterated the mischaracterizations of employment made in respondents' recruitment advertisements. Inaccurate job descriptions given during initial interviews included: public relations work (Kolkhurst 10017-18); promotional advertising, which included placing encyclopedias or other educational materials in the homes of individuals selected to participate in an advertising campaign (Dennen 9270, 9289; Williams 9340; Tepker 9438-39, 9441; O'Hara 9998; Miller 10167-68; Hanke 10419, 10447; Evans 10609; Thorn 11160-61; Walker 11216, 11235-36; McNamara 11271; Davenport 11707; 11711; McWilliams 11995-98); discussing educational plans with families and awarding [37] prizes (Will 9596); distributing free vacation certificates and taking an opinion poll (Kellogg 10296-97); or, interviewing prospective members of a Mothers' Club (Gribbin 13120-21).

75. Many of respondents' new sales employees did not realize that their job was to sell encyclopedias until training was actually in progress or had been completed (Dennen 9289, 9292-93; Williams 9369; O'Hara 9998; Kolkhurst 10035; Miller 10192; Kellogg 10319-20; Russell 10387; Thorn 11184; Walker 11214-15, 11235-37; Latasa 11802-03; Howard 12906). Their misconceptions as to the nature of

their employment persisted despite the fact that a "sales" presentation, which they were to use, was frequently given at their initial interviews and taught to them during training (Hanke 10419, 10447-48; Walker 11235-36). Rather than dispelling new employees' misconceptions, the content of these sales presentations reinforced the impression that new employees were engaged in work other than door-to-door sales of respondents' products (Evans 11707).

76. Many of respondents' new employees were explicitly told that their jobs did not involve selling (Dennen 9289-90; Hanke 10419, 10447; Evans 10646; McWilliams 12036; Gribbin 13120, 13159). In other instances, although affirmative misrepresentations were not made, the words "sales" or "selling" were never used during training, and new sales employees remained uninformed as to the true nature of their employment (Tepker 9446; Will 9597; Walker 11234; Westheimer 11499).

(2) Compensation Guarantees

77. As discussed *supra*, blind recruitment advertisements placed by respondents frequently contained income or salary guarantees (see Finding 68). Although respondents maintain that salary "guarantees" were fully discussed with all applicants during their initial interviews (Covens 13726; McClearey 13931-32; Loots 14671), many new employees did not receive a full explanation as to the availability of or conditions placed upon receipt of a "guarantee" until they had begun training or were actually selling in the field (Kolkhurst 10018, 10041-42; Thorn 11161-62, 11187; Westheimer 11438; Gribbin 13129-30; see also, Dennen 9294; Williams 9344; Miller 10172-73; Kellogg 10303). [38]

78. Commissions on accepted sales and "guarantees" were the two compensation formulas used by respondents for new sales representatives (Dennen 9294; Williams 9340; O'Hara 9981, 10005; Kolkhurst 10042; Latasa 11803; Howard 12897). Under the commission plan, a stipulated sum or percentage per placement was paid (Will 9555; Waugh 10498; Evans 10610). The operation of the "guarantee" plan varied. Under the terms of some guarantees, sales representatives were paid the difference, if one existed, between sales commissions earned and the amount guaranteed (Culver 12943, 12964; Mawle 14810). Other "guarantees" were represented as being a straight salary plan which bore no relationship to placements made. Under this plan, if a salesman's commissions exceeded the guarantee, he was paid only the sum guaranteed (McNamara 11272).

79. Applicants responding to blind recruitment advertisements which contained a guarantee were sometimes required to choose

between the two compensation plans after they had been discussed (Kolkhurst 10042; Miller 10173; Evans 10610; McNamara 11272; Latasa 11803). In other cases, despite the advertisement representations, new employees were informed during their initial interview or training that straight commissions was the only method of compensation available to them (Will 9596; O'Hara 10005; Kellogg 10303, 10320-22). In cases where new employees were given a choice as to the method of compensation, a written employment agreement setting forth their choice was sometimes executed (CX 968; RX 31, 41 Tepker 9471; Miller 10173; Hanke 10420; Culver 12943; Covens 13651; McClearey 13936; Loots 14677; McKean 15082; Toman 16296).

80. If new employees were given a choice between commissions and a guarantee, subtle persuasion and "encouragement" was frequently applied to talk them out of choosing guarantees (Vaughn 5925; Dennen 9294-95; Williams 9345; Kellogg 10303, 10321; Hanke 10421, 10456-57; Evans 10679; Latasa 11803-04, 11875). If they resisted this "encouragement," increased pressure was applied to ensure that the chosen method of compensation was the commission plan (Russell 10388; Howard 12897, 12904).

81. An additional impetus to ensure that most new employees would opt for the commission plan was representations made by respondents that commissions due on sales almost always exceeded the guarantee (CX 563T; Havas 9202, 9229; Williams 9345; O'Hara 10006; Kellogg 10322; Russell 10388; Westheimer 11479; McWilliams 12001; Covens 13727; Basilici 14929). New employees were assured [39] that they could *easily* earn more under the commission plan (Dennen 9294; Johnson 9530-31; Waugh 10498; Evans 10610). Some new sales representatives under the commission plan, did, in fact, exceed the amount of the guarantee (Gilbow 12221; Loots 14677-78). The majority of new sales employees, however, did not earn commissions which approximated the income they had been led to anticipate (Havas 9229-30; Kolkhurst 10046; Miller 12794; Culver 12973).

82. When new sales employees commenced work under a guarantee, receipt of such guarantee was normally conditioned on giving a specified number (*e.g.*, 48), of complete, authorized presentations per month[22] (Thorn 11162; Westheimer 11439; Miller 12794; Culver 12943; Covens 13647, 13651, 13724; McClearey 13932-33; Loots 14671, 14677, 14681; Mawle 14787). Cards which reflected presentations given were filled out and turned in by sales representatives seeking to qualify for a guarantee (Williams 9345; Tepker 9451;

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[22] At times, a minimum number of placements, *i.e.*, 3/wk., was the condition placed on receipt of a guarantee (Latasa 11804; Storms 13331-34).

Kolkhurst 10019, 10042; Thorn 11162; Walker 11226; Miller 12794; Culver 12943; McClearey 13933–34; Loots 14677).

83. Respondents maintain that the number of presentations required to qualify for a guarantee was realistic and that new employees could easily fulfill this condition (Evans 10610; Davenport 11712; Covens 13651–52; McClearey 14004; Loots 14681; Basilici 14929–30). In actuality, giving the required number of complete presentations proved extremely difficult due to the length of time required for each presentation. Failure to fulfill this condition was the major reason many new employees did not qualify for guarantees (Tepker 9451–53; Walker 11226–27, 11239; Westheimer 11439–40; Davenport 11713–14; Gilbow 12196–98; Miller 12795; Culver 12975). In lowering the set number of presentations required to qualify to 40, respondents cited the difficulty encountered in trying to make 48 presentations (McClearey 13932–33).[23] [40]

84. Respondents' official policy was to pay the advertised guarantees when the conditions attached thereto had been met and, in accord with this policy, some guarantees were paid (RX 60, 504; Covens 13648–49, 13652; McClearey 14005; Mawle 14787–88; Basilici 14929; Ryan 15941, 15943, 15951).[24]

85. In addition to omitting conditions placed on guarantees, no time limit on the duration for payment of such guarantees was expressed in the blind recruitment advertisements placed by respondents (see Finding 59). However, respondents' practice, which apparently reflected corporate policy, was generally to make such guarantees for only the first month (CX 960; Covens 13728–29; Mawle 14810; Basilici 14947; Ryan 16036, 16049).

86. Under the commission plan, a reserve for cancelled orders was created by deducting a set sum from each commission (CX 784B; Snyder 8792, 8796–97; Hanna 13193). Other deductions were also made for sales kits and materials and increased publication costs (Williams 9357; O'Hara 10037; Hanna 13208). Many new sales representatives were not informed that such deductions would be made from commissions until training had been completed and they were working in the field. They also were not advised that amounts withheld would not be refunded upon termination of their employ-

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[23] "Q. What was wrong with the 48?

A. We felt that it was too many presentations for the man to be able to make without having to force him to work on Sunday or something straight through seven days a week.

Q. They had a difficult time making 48 presentations?

A. Yes" (McClearey 13932).

[24] RX 504, a chart of guaranteed salaries paid by Richards from 1967–1971, lists paid guaranteed earnings totalling $252,544. The fact that some payments were made under a guarantee program, however, does not preclude a finding that such guarantees were not available to all individuals responding to "guarantee" recruitment advertisements.

ment (Snyder 8726-27; Kellogg 10316; Thorn 11193). In fact, affirmative misrepresentations were made to some new employees that they would be paid such withholdings when they left respondents' employ (Waugh 10519, 10527; Miller 12796, 12821; Hanna 13193, 13209).

87. In the course of their work, some sales representatives incurred expenses for travel, motels and food. Although they had been led to believe such expenses would be paid by respondents, they were not reimbursed for these expenses (Kolkhurst 10046; Walker 11228, 11250-51; McWilliams 12018, 12052, 12056; Miller 12812). [41]

88. Representations regarding "guarantees" made by respondents during the initial interviews and training of new employees were deceptive in that:

(1) guarantees were not available to all new employees nor were they usually paid for more than one month;

(2) the conditions placed upon receipt of guarantees were not easily fulfilled;

(3) pressure to convert to commissions was frequently exerted; and

(4) representations that earnings under the commission plan would exceed guarantees did not reflect the usual experience of new sales representatives.

The limitations and conditions placed upon receipt of a guaranteed salary were material facts which would have affected a prospective employee's decision to respond to respondents' recruitment advertisements. Failure to disclose these facts was, therefore, false, misleading and deceptive.

IV. SALES PRACTICES

A. *Introduction*

89. Respondents' sales representatives are trained to sell the publications and services retailed by respondents in combination rather than individually. A combination usually consists of a single major publication (encyclopedia) and various premium items (CX 9C). The respondents distribute standard combination schedules to their respective sale representatives which set forth the various publications to be included in each combination and the price for each such combination (CX 9-13B). As additional items are included in the combination offer, the combination price increases (CX 9A).

90. The Executive Committee of Grolier, Inc. designated which direct selling subsidiaries would have distributional rights to each

publication sold (see Finding 34). The following table sets forth the publications sold by respondents for the calendar year 1969: [42]

Products	*Major Sets*	*Respondents Who Sold Products*
[25] 1.*	Encyclopedia Americana 30 Volumes	Americana, Grolier Interstate
2.*	Encyclopedia International 20 Volumes	Grolier Society, Spencer, Grolier Interstate, Grolier New Era
3.*	New Book of Knowledge 20 Volumes	All named respondents
4.*	World's Greatest Classics 50 Volumes	Americana, Grolier Society, Spencer, Hinkley, Grolier Interstate, Grolier New Era
5.*	Collegiate Encyclopedia (Exactly same as Encyclopedia International except in different binding for students) 20 Volumes	Hinkley, Grolier Interstate
6.*	Grolier Universal Encyclopedia, 10 Volumes, based on information gathered for Encyclopedia International	Grolier Society, Spencer, Hinkley, Grolier Interstate, Grolier New Era
7.*	American People's Encyclopedia	Richards, Madison
8.**	Harvard Classics	Americana, Grolier Society, Grolier Interstate, Grolier New Era, Hinkley, Spencer [43]

Premiums		*Respondents Who Sold Products*
[26] 1.*	Our Wonderful World 18 Volumes	Americana, Grolier Interstate, Grolier Society, Spencer, Hinkley
2.*	The Book of Art 10 Volumes	All named respondents
3.*	Basic Home Library	All named respondents
4.*	Book of Popular Science, 10 Volumes	All named respondents

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[25] Where one asterisk is shown, the product is published by Grolier, Inc.; where two asterisks are shown, the product is not published by Grolier, Inc.

[26] Where one asterisk is shown, the product is published by Grolier, Inc.; where two asterisks are shown, the product is not published or manufactured by Grolier, Inc. (CX 8a–f).

Products		*Respondents Who Sold Products*
5.*	Lands and Peoples 7 Volumes	All named respondents
6.*	Thru Golden Windows 10 Volumes	Richards, Madison
7.*	Children's Hour 16 Volumes	Grolier Society, Spencer, Hinkley, Grolier Interstate
8.*	Grolier Classics 10 Volumes	Grolier Society, Spencer, Hinkley, Grolier Interstate
9.*	Yearbooks	All named respondents
10.*	Research Service	All named respondents
11.**	Teaching Machine – Min/Max and Programmed Courses	Americana, Grolier Society, Grolier Interstate, Hinkley, Spencer, Richards
12.**	Bookcase	All named respondents
13.**	Medical Encyclopedia	Americana, Grolier Society, Grolier Interstate, Hinkley, Spencer, Richards, Madison
14.**	Bible	Americana, Grolier Society, Grolier Interstate, Hinkley, Spencer, Richards, Madison
15.**	Dictionary	Americana, Grolier Society, Grolier Interstate, Hinkley, Spencer, Richards, Madison [44]
16.**	Hammond Atlas	Americana, Grolier Society, Grolier Interstate, Hinkley, Spencer, Richards
17.**	Bookshelf for Boys and Girls	Americana, Grolier Society, Grolier Interstate, Hinkley, Spencer

B. *Lead-Generating Activities*

(1) Parochial and Private School Promotions

91. In the course and conduct of its business, a primary technique used by respondent Spencer to obtain leads to potential customers was to contact parents of parochial schoolchildren through the private schools they attended. This technique spread from Boston and New York through the south, central and southwest United States as early as 1968 (Basilici 14907, 14940–41).[37]

92. Initial contact seeking permission to give various materials to

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[37] Respondent Grolier Interstate currently uses a lead-getting technique in parochial, private schools and preschools (RX 533A-Z-161; Mawle 14793; Toman 16243).

the schoolchildren to take home to their parents was made with the principal of a parochial school by telephone. Spencer salesmen followed a standard "telephone talk" which they had been instructed to use verbatim during this call (CX 787A; Snyder 8732-33; Havas 9210). The caller identified himself as being with the National Institute of Programmed Learning, which is engaged in work of a public service nature designed to foster the use of programmed learning in the schools. This avowed affiliation was intended to elicit a favorable response from individuals contacted. Respondents submitted no evidence that such an institute actually existed or that, if it did, Spencer had any affiliation with it (Snyder 8817-18; Havas 9211-12, 9258-59). In some instances, Spencer Salesmen stated they were working for the National Catholic Educator's Association (Roepke 9178, 9186). Reference was also made to "rave reviews" for respondents' programmed learning received [45] from sisters attending the National Catholic Educators convention (CX 787A; Snyder 8818-19).

93. Spencer salesmen contacting parochial school principals would inform them that:

> a letter has been composed by many of your leading educators, explaining the benefits of Programmed Learning which we have just distributed free, as a public service, to the public school children and we are presently distributing these announcements through the Parochial Schools.

They would further represent that these announcements were being distributed by volunteers from Catholic universities or local colleges (CX 787A; Snyder 8736).

94. Arrangements were sometimes made for a personal meeting with the school's principal prior to distribution by volunteers of Spencer's materials (Roepke 9179-80). In other instances, no such meeting was set and arrangements for volunteers to drop off the materials to be sent home with the schoolchildren were made during the initial phone call (CX 787A; Dominic 8876, 8884-86). The volunteers who delivered distributional materials to the schools were, in fact, Spencer salesmen who had been instructed to fend off inquiries by stating that, as volunteers, they knew nothing about the program or materials they were distributing (Snyder 8736; Havas 9210, 9252-53).

95. As a result of the initial phone call or meeting, principals of parochial schools believed that the purpose in contacting pupils' parents was to take a poll or develop interest in getting Federal support to obtain Spencer's programs for use within the parochial schools (CX 1544; Roepke 9182, 9188, 9192-96). The official response

to any objections or questions by a principal questioning whether sales or solicitation was the underlying motive for contacting the parents was:

> Oh no, sister, this is completely different. Nobody would be contacted directly or indirectly as a result of our work.

(CX 787B.)

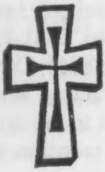
[46] (See also Roepke 9180, 9191). Implicit representations that Spencer's contact with the school had been cleared or approved by the archdiocese were also made (CX 787B; Roepke 9188–89; Gaffney 13003, 13029–32). For example, when asked whether diocesan approval had been given, respondents' representatives were instructed to say:

> Oh no, Sister this is completely different. As a matter of fact, because this program is of such an unusual nature, naturally they wouldn't send a letter out directing you to distribute these announcements. However, we have been told that this is to be left up to the discretion of the individual principals.

(CX 787B.)

96. Parochial school principals who agreed to distribute Spencer's programmed learning and speedreading materials were not aware at the time of distribution that other products such as encyclopedias were involved nor did they intend to endorse any products sold by Spencer (CX 1544; Dominic 8875–76, 8892; Roepke 9179–80, 9183; Gaffney 13007–10).

97. The materials left with the schools for distribution to parents were enclosed in an envelope with the following legend:



IF YOU PLAN ON SENDING
YOUR CHILDREN TO COLLEGE,
READ THIS IMPORTANT
INFORMATION.

THEN, RETURN TO CLASSROOM
TOMORROW—SIGNED OR UNSIGNED . . .

(CX 788)

[47] The bold cross in the upper left-hand corner was used to make it appear that the packet had originated with the school or diocese so

that parents would be more inclined to examine it (Havas 9211). Included within the packet distributed to parents was a letter promoting either Spencer's programmed learning or automated speedreading programs (CX 789, 791) and a request card for a free demonstration to be filied out and returned by the parent (CX 790, 2086).[28] No mention of Spencer or encyclopedias is made in any of these materials.

98. Parents receiving the packets described in the preceding finding frequently thought such materials and the programs discussed therein had been reviewed and approved by the school prior to distribution (Tiburcio 8657, 8659, 8697; Canario 9122, 9180-81; Stasiunas 15823-25). Parents of parochial schoolchildren receiving commercial material sent home through the schools will frequently assume such material has been reviewed and endorsed by the school (Dominic 886-87; Gaffney 13008-09, 13015, 13033, 13039-40, 13043-44). No disclosures were made by Spencer's sales representatives to obviate such misunderstandings and, in fact, the content and format of the materials sent to parents tended to reinforce the impression that the school had endorsed respondents' products (*e.g.*, CX 788; Finding 97).

99. After the cards (CX 790) had been filled out and returned to the schools, employees of Spencer, again posing as "volunteers" would pick them up (Dominic 8886; Havas 9214). Parents who returned these cards were subsequently contacted by phone to set up an appointment for a free demonstration. When parents asked if the schools had endorsed the programs presented, Spencer salesmen sidestepped with responses such as "Well, the material did come from the school, didn't it?" (Havas 9208.) [48]

100. CX 793 and 871V are representative of the telephone talks Spencer employees used when contacting parochial school leads. Salesmen were instructed that Spencer policy dictated that they follow these prescribed talks verbatim (Snyder 8737-38, 8845; Havas 9214-15; Hanna 13211-12). Contacts were told an "instructor" would be in their area that evening and that the caller wished to set up an appointment for a 10-minute free demonstration.[29] No mention was

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[28] Spencer salesmen explained to principals that the discrepancy in stated purpose between CX 790 (to give a free demonstration) and their poll of parents for Federal support was because they had not had time to develop new forms and were using CX 790 in the interim (Roepke 9180).

[29] CX 871V stated in part: ". . . AS YOU KNOW, WE AGREED TO GIVE EACH FAMILY A FREE DEMONSTRATION ON PROGRAMMED LEARNING AS A PUBLIC SERVICE, AND THE REASON I'M CALLING NOW IS THAT OUR INSTRUCTORS WILL BE IN THE *(Name)* AREA TONIGHT. I THOUGHT I'D CALL FIRST TO MAKE SURE BOTH YOU AND MR. ________ WILL BE IN THIS EVENING. IT TAKES AROUND 10 MINUTES, SINCE EACH INSTRUCTOR SEES ABOUT 6 OR 7 FAMILIES AN EVENING. NOW, WILL BOTH YOU AND YOUR HUSBAND BE IN THIS EVENING, BETWEEN SAY, 6:30 - 7:30, OR WOULD 7:30 - 8:30 BE MORE CONVENIENT? FINE. (Check address and nearest street corner.) OUR INSTRUCTOR WILL LOOK FORWARD TO SEEING YOU BOTH AT ________ (Mention the appointment time.) THANK YOU."

made of Spencer encyclopedias or the underlying solicitation purposes of the demonstration. Irrespective of how the lead was generated, the sales presentation subsequently given was essentially the same.

101. Representations made by respondent Spencer in contacting parochial schools and the parents of children attending these schools were false, misleading and deceptive in that:

(1) the purpose of such contacts has been represented as something other than the solicitation of sales; and

(2) the method of transmitting promotional material to parents and the content of sales presentations had the capacity to lead parents to believe that the program offered had been reviewed, approved or endorsed by the parochial schools or archdiocese.

(2) National Advertising Promotions

102. In the course and conduct of its business, Grolier, Inc. has placed advertisements in magazines of national circulation in order to obtain leads who could be contacted by its home subscription subsidiaries for the purpose of sales [49] solicitation (Romano 682; Mawle 3474-75; Waller 5793-95). These advertisements were placed in such prominent magazines as *Life, Look, Redbook* and *Good Housekeeping* (CX 1612A-D).

103. The following are illustrative of the coupons contained in the national advertisements placed by respondents to generate leads:

> The New Book of Knowledge Putnam Valley, New York 10579
>
> Please send me my free copy of your color booklet, "The Magic Carpet." There are _____ children in my family, ages _______________
>
> Name ____________________________________
> Address ____________________________________

(CX 1611H.)

> The New Book of Knowledge Putnam Valley, New York 10579
>
> Please send me my free copy of your booklet, "The Magic Carpet." There are _____ children in my family.

* * * * * * *

> Also available: Free 16 page bonus booklet, "To the Moon and Beyond" (Supply limited)

(CX 1612E.)

> [50] Encyclopedia Americana Putnam Valley, New York 10579
>
> Please send me "Eyewitness to Achievement," your full-color booklet packed

with information that explains how the readable Americana helps children and adults to further knowledge.

* * * * * * *

Enter our Americana Poll. It might win you a set of the Encyclopedia Americana for free.

(CX 1613H.)

(See also CX 1611J-K, 1612F and 1613J-K.) Readers were requested to fill out and mail these coupons to get the free booklets offered.

104. Respondents' purpose in soliciting return of the above coupons was to obtain leads to prospective customers. After the booklets requested had been mailed, the coupons were sent to the sales office located nearest to the prospect (Waller 5793-94). Sales representatives thereafter contacted these individuals by phone to set up an appointment at which a standard sales presentation (discussed *infra*) was given (Romano 682; Long 2848; Mawle 3475).

105. Respondents' national advertising to generate leads was deceptive in that it failed to disclose the material fact that individuals submitting the appended coupons would be contacted by a sales person for the purpose of soliciting the sale of respondents' products.

(3) Store Promotions

106. In the course and conduct of their business and for the purpose of generating leads to prospective customers, respondents established booths in stores soliciting store customers to enter a drawing for a "free vacation" by filling out an entry card (Johnson 9514-15; Thorn 11169). [51]

107. All entrants in the drawing who qualified as prospective customers were subsequently informed by telephone they had won a free vacation and an appointment was made to award their vacation certificate. This representation was false, misleading and deceptive in that no drawing had been held and the real purpose in obtaining drawing entrants was to solicit the sale of respondents' products (Johnson 9515; Thorn 11169).

C. *Telephone Solicitation*

108. Respondents sometimes made initial contact with prospective customers via prepared "telephone talks" aimed at setting up appointments with such individuals. Although the content of these "talks" varied, they were all designed to convey the impression that

the purpose of the in-home appointment was something other than the sale of respondents' products of services.

109. Individuals contacted were frequently told they had won a free vacation (CX 448B; Johnson 9515; Miller 10174; Culver 12945), Min/Max Teaching Machine (Murphy 8850-51; Williams 15876), or art reproduction (CX 452; Mawle 3457-58; Will 9560-61) and that the purpose of the telephone call was to set up an appointment to award their prize certificate. Names of such "winners" were compiled from telephone directories (Will 9557-58; Kellogg 10302; Gilbow 12127) and from cards submitted as a result of national advertisements (Findings 102-05; Mawle 3457-58) or the contest display booths set up in department stores (Findings 106, 107; Johnson 9515).

110. Free vacation certificates were also given to individuals contacted by phone regarding respondents' Consumer Buying Service.[30] Prospective customers were told that, if they would attend a meeting to learn about how they could save money on purchases through Consumer Buying Service membership, they would receive a free vacation certificate or gift (Lay [52] 9733; Hatcher 10859-60; Larsen 11406; Kearns 11909, 11912; Clarke 12575). The fact that one of the main purposes of such meetings was to sell respondents' publications was not disclosed at the time the first contact was made with the prospective student customers (Lay 9733; Hatcher 10860).

111. Another form of "telephone talk" used by respondents informed prospective customers that they were being considered for or had been selected as a sponsor or promotional family and could receive new products marketed by respondents. An appointment was set up so that a company representative could explain the details of being a selected household to individuals contacted (CX 563I and O; Will 9558-59; Clarke 10335; Ford 10559-60; Evans 10625-27).

112. Respondents' "telephone talks" assured contacts that no obligation was incurred and that the appointment would not involve solicitation of sales of respondents' products (CX 563I and O; Murphy 8851; Johnson 9515; Will 9558).[31]

113. Such "telephone talks" used by respondents were false,

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[30] In some instances, individuals received a card or letter in the mail with a telephone number to call to obtain the vacation certificate and information regarding the Consumer Buying Service (Larsen 11404; Krubsack 11943).

[31] ". . .but please do not be alarmed Mr/Mrs ____________ because *I didn't call you to give you a sales talk!* The purpose of my call is this:

"Grolier has approximately 7000 sales people across the country and we have to provide these sales people with prospects to call on. Right now we are getting some help from several families in each community and in return for that help we are paying these families in Grolier merchandise.

• • • • • • •

"If prospect says they are not interested - say 'That's fine - all I want to do is explain what we are doing and like I said I am not coming out there to give you a sales talk' " (CX 563I).

misleading and deceptive in that they affirmatively misrepresented that the purpose of the in-home appointment was *not* to solicit the sale of respondents' products and services.

D. *Door-To-Door Solicitation*

114. Standard introductory talks or "door-openers" were used by respondents in their initial contact with prospective customers in their homes. Although the precise language of these "door-openers" varied, the content and purpose, *i.e.*, to gain entry to the home, remained constant. [53]

115. "Cold canvassing" is a method whereby sales representatives make initial contact with prospective customers in their home without prior notification of their visit and where the persons contacted have not indicated a prior interest in respondents' products or services. This is a technique of establishing contact with prospective customers which respondents' home subscription subsidiaries used extensively (Ryan 16075). Various "door-openers" or door approaches were used in this endeavor.

116. When following up on appointments generated through telephone solicitation, respondents' sales representatives used standard door-openers which coincided with the telephone representations made, *e.g.*, delivery of a prize certificate (CX 419A, 446A, 448A; Kellogg 10298–99).

117. In one frequently used approach, prospective customers who had not previously been telephoned were informed at the door that the caller's purpose was to award a prize or certificate such as the vacation gift certificate. After the awarding of prizes, prospective customers were told that, in addition, they were eligible to enter an opinion poll contest to win a free set of encyclopedias or the New Book of Knowledge (CX 446A, 446C, 488A). Prospective customers were told that the purpose of the opinion poll contest was to ultimately use winners' names and opinions in an advertising campaign to publicize respondents' educational materials. In addition to being eligible to enter the opinion contest, a special opportunity was extended to individuals contacted to obtain the educational program described, without the usual costs, for additional help and cooperation (CX 419C, 446, 447B). This help and cooperation took the same forms discussed, *infra* (Findings 144–49).

118. Another prevalent theme used by respondents' sales representatives in "cold canvassing" characterized the purpose of the contact as an interview or survey in conjunction with a product promotion program (CX 821A, 871F, 964B; Dennen 9274; [54] Tepker

9442–43; Warwick 9670; Fjelstad 9821). Examples of these door-openers include phrases such as:

> . . . I AM DOING PRODUCT PROMOTION WORK FOR SPENCER INTERNATIONAL . . . MOST PEOPLE WE TALK WITH DON'T ASSOCIATE THE NAME INTERNATIONAL WITH ANY SPECIFIC PRODUCT AND THAT'S WHY WE ARE CONDUCTING THESE INTERVIEWS . . .
>
> * * * * * * *
>
> . . . WE'RE NOW WORKING ON A MORE DIRECT TYPE OF SALES PROMOTION TO BACK UP OUR NATIONAL ADVERTISING. IT IS GOING TO EFFECT FAMILIES IN EACH AREA, LIKE YOURSELF. IT IS A PRODUCT PROMOTION DESIGNED TO STIMULATE "WORD-OF-MOUTH" RESPONSE . . . SO SPENCER HAS DEVELOPED A VERY UNIQUE AND UNUSUAL PROMOTION CAMPAIGN ON A MUCH MORE LIMITED SCALE. SPENCER IS ACTUALLY GOING TO BE OFFERING THE NEW INTERNATIONAL TO QUALIFIED FAMILIES IN EACH AREA _____ IT WOULD BE THEIRS TO KEEP FOREVER AND OF COURSE THAT'S PUT IN WRITING!

(CX 821B.)

> . . . I've been asked to interview a few families on a new program about to be released in the area. It involves asking you and your wife a few impersonal questions and it just takes two minutes

(CX 958.)

> Hi, I've been asked to call on you . . . I have to interview everyone. . . .
>
> As I said, I am with the public relations and advertising division of my company . . . Now we are setting up our local advertising in order to get local support. This is why I am here this evening. You see, the type of advertising we are interested in on a local level is letters of opinion and testimonial letters from satisfied owners telling us what they think of the product. . . .

(CX 1023A.)

[55] 119. Following such introductions, potential customers were asked for their responses to a brief list of questions provided to salesmen by respondents (CX 821A, 871F). Dummy IBM cards following the questionnaire format were sometimes filled in by respondents' sales representatives (Miller 12800). When asked about the cards, sales representatives were instructed to say that the information would be fed into computers thus implying it would be used in a marketing research effort (Miller 12833). The record, however, demonstrates that the purpose of the questionnaire was to gain entry to the home and determine if the prospect met respondents' credit standards (Kotler 5069–70; Miller 12800–01). No other use was made of the information elicited through the

"interview" or "survey" or recorded on the IBM cards (Waugh 10536–37; Westheimer 11441–42, 11481; Miller 12802, 12833).

120. After completing the questionnaire, respondents' sales representatives would discuss product promotion, the failure of national advertising to effectively promote respondents' "pre-school through college home reference library" and their endeavor to work on:

> A MORE DIRECT TYPE OF SALES PROMOTION TO BACK UP OUR NATIONAL ADVERTISING . . . . A PRODUCT PROMOTION DESIGNED TO STIMULATE "WORD-OF-MOUTH" RESPONSE.
>
> * * * * * * *
>
> A VERY UNIQUE AND UNUSUAL PROMOTION CAMPAIGN . . . SPENCER IS ACTUALLY GOING TO BE OFFERING THE NEW INTERNATIONAL TO QUALIFIED FAMILIES IN EACH AREA _____(CX 821E; for additional examples, see Finding 118).

121. Having gained access to prospective customers' homes through a survey/interview door approach, respondents' sales representatives would give one of the standard sales presentations described in subsequent findings.

122. In their initial contact with prospective customers, sales representatives of respondents' Grolier New Era and Grolier Society sought to enroll mothers in a "Mothers Club" (Gribbin 13121; Storms 13303). The stated purpose of this club was to provide middle class families with the necessary tools to ensure that their children would have a well-rounded [56] educational program (CX 618D). In actuality, respondents' sales representatives were not offering membership in a club since no bona fide club existed. This device was used solely for the purpose of selling respondents' publications and services (Vaughn 5877, 5897).

123. The survey door approach was also used in connection with the Mothers Club sales presentation (Vaughn 5876–79). The standard door-opener used in this presentation was:

> Good morning, I am Jane Smith, a field counselor with the New Era Young Mothers Club assigned to your community. I am making a field report for the club and acquainting the mothers in this area with its work and explaining its benefits and privileges. As part of my work I am requested to send field reports to my office. I would very much appreciate your cooperation in answering just a few questions relating to child education.

(CX 2087D.)

(See also CX 618B; Gribbin 13123; Storms 13305.)

124. After delivering an introductory talk similar to that set forth above, the sales representative utilizing the Mothers Club presentation would fill out what was called a field report by asking the customer a series of questions concerning the prospect's family and children (CX 2044, 2091;[32] Vaughn 5912; Gribbin 13123). The primary use of such survey was as a lead-in to the sales presentation (Storms 13305–06). [57]

125. At the conclusion of the field report, the Mothers Club sales representative would state: [58]

> Mrs. Prospect, you have been very gracious spending this time answering these questions, they are important to us and will be forwarded to my company, whose headquarters are in New York. Are you at all familiar with the work of the New Era Young Mothers Club.

(CX 2087D; see also 618C.)

At this point, the sales representative began one of the standard sales presentations discussed *infra.*

E. *Misrepresentation of or Failure To Disclose Purpose of Initial Contact*

126. Respondents' official policy prohibited misrepresenting to a prospective customer the purpose of a telephone call or home visit (RX 63A, 69B; McKean 15490, 15492). In fact, some corporate directives explicitly provided that a full disclosure be made as to the purpose of the call or visit and the identity of the caller (RX 65A, 68A).

127. Experienced salesmen employed by respondents and their corporate officials expressed a reluctance to affirmatively disclose at

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[32] "NEW ERA YOUNG MOTHERS CLUB FIELD REPORT

"I'm with the Young Mothers Club, making a field report. How many people live here? ______

Children ______ Adults ______ Ages ______

School: Public ______ Parochial ______

"1. Which do you feel are the most impressionable years of a person's life? Childhood ______ Adolescent ______ Adult ______

2. Who do you feel has more influence on the children? Mother ______ Father ______ Teacher ______

3. Which area of environment do you feel has more basic influence on the children? Home ______ School ______ Church ______ Street ______

4. Are you familiar with the following. . . A. New Pre-School training methods? Yes ——— No ——— B. Modern Math: eg. Pyramid system or new math? Yes ——— No ——— C. Are you aware of a shortage of good teachers? Yes ——— No ———

5. Do you have the following materials in your home? Educational Toys? ——— Children's Magazines and Stories? ——— Dictionary? ——— Reference Materials? ——— Bible? ——— Educational Recordings? ———

6. Have you ever had any phone calls regarding this information? Yes ——— No ———

7. You do have a phone, don't you? Yes ——— No ———

8. I don't suppose you work, but what kind of work does your husband do? ______

9. How do you spell your last name? Name ______

10. I know we're on ______ Street, but what's the number? ______

11. Are you familiar with the work of the New Era Young Mothers Club?" (CX 2044, 2091.)

the outset, the sales purpose of such contacts (McClearey 14008-09; Goldstein 14132; Stearns 14624-25; Loots 14705-06; Basilici 14925-26). Aware of many prospective customers' aversion to dealing with door-to-door encyclopedia salesmen, respondents' representatives sought to delay disclosing the sales purpose of their contact until this natural resistance to being sold was diminished, the stage had been set and it would no longer be "too easy for [the] individual to say . . . [W]e have some" (DeLucia 15073; see also David 13559-61).

128. None of the standard "telephone talks," "door-openers" or sales presentations used by respondents' sales representatives used the word "sales" nor did they inform the prospective customers that the objective of the contemplated transaction was the sale of respondents' encyclopedias and other educational materials (CX 419, 446, 447, 448, 563H, 563I, 563"O", 786, 821, 871). [59]

129. Respondents' sales representatives were instructed not to mention encyclopedias at the door (Thorn 11170) and to avoid using the word "sale" during the sales presentation (Dennen 9289-90; Kolkhurst 10020; Westheimer 11497; Storms 13303, 13315). Sales representatives were trained to affirmatively misrepresent the purpose of their contact with prospective customers by characterizing such contact as an interview, survey or club enrollment. If questioned as to a sales motive, they were instructed to explicitly deny any intent to solicit sales of respondents' products or services (Havas 9206, 9218; Dennen 9279, 9302; Williams 9346-47; Tepker 9446; Johnson 9515; Will 9558; Evans 10707-10; Walker 11241; McWilliams 12000-03; 12075; Gilbow 12128, 12137, 12311; Storms 13303).

130. In some sales presentations, the retail installment contracts used by respondents' sales representatives were referred to as "receipts," "guarantees" or "shipping forms" (Dennen 9285-87; Will 9589; Miller 10185-86; Hanke 10433-34; McWilliams 12012-14). Such designations reinforced the erroneous impression conveyed to prospective customers that the purpose of the presentation was not the solicitation of sales of respondents' publications and services.

131. Some customers were able to discern, either from materials received through the schools, the content of telephone calls setting appointments or responses to their questions, the sales purpose of respondents' contact (Shaw 14576; Clapp 14635-36; Ferguson 14953-54; Connors 15324-25; Thompson 15589, 15602; McConnell 15783-84; Stasiunas 15834; Williams 15876-77). The representations utilized in connection with the initial contact with the consumer, nevertheless, had the capacity to mislead (Findings 91-130).

132. The purpose of respondents' sales representatives' contact,

which is to sell, is a material fact in a prospect's decision to let such representative into their home. The failure to disclose at the outset, and in many instances, to affirmatively misrepresent, the purpose of contacting prospective customers was false, misleading and deceptive (see Findings 91-130). [60]

F. *Representations as to Duration of the Sales Presentation*

133. During the initial contact, whether made by telephone or at the door, respondents' sales representatives stated that the entire visit, whether characterized as a survey, interview or awarding of prize certificates, would take only a few minutes of the contact's time (English 531; Tiburcio 8660-61; Murphy 8851; Johnson 9525; Will 9559; Warwick 9670; Halsey 9691; Nesper 9784; Laundre 9954; O'Hara 9984; Kellogg 10301; Waugh 10506; Westheimer 11441; McWilliams 12000; Miller 12800; Ivaska 13227; Goldstein 14089; Basilici 14912). Similar statements as to the minimal time required for such visits were contained in the standard presentations used by respondents' sales representatives (CX 448B, 956A, 958).

134. In contrast to the above representations, the time required to give a standard sales presentation normally exceeded one hour (English 531; Snyder 8753; Canario 9134; Johnson 9545; Will 9589; O'Hara 10001; Kolkhurst 10034; Westheimer 11439, 11458; Miller 12811; Reames 13349; Goldstein 14090; Shaw 14578; Clapp 14640; Basilici 14913, 14925; Thompson 15603; Stasiunas 15806; Williams 15885).

135. In deciding to permit respondents' sales representatives into their homes, the time required for such visit was a material fact. Given the disparity between the time representation made to prospective customers and the anticipated time of a sales representative's visit, such representations as to the duration of the call were misleading.

G. *Training in Use of Standard Presentations*

136. Respondents disseminated prepared telephone talks, door-openers and sales presentations to new employees to use when contacting prospective customers (CX 419, 447, 618, 651, 821, 871, 958, 1023; Ryan 5814-15, 16026; Pardee 11103-04). Respondents' sales representatives were trained to use these materials (Miller 10168; Westheimer 11438). For example, respondent Spencer's Training Manual admonished new sales representatives to:

> FOLLOW PRESENTATION - *Do not deviate* - it must be done our way, which is the successful way.

(CX 871B.)

[61] 137. During training, respondents' new employees were either given written versions of the presentations they were to use, given authorized presentations to copy over for their use, or instructed to copy down such presentations as they were given orally by trainers (Tepker 9441; Johnson 9513, 9538; Kolkhurst 10018; Miller 10168, 10170; Kellogg 10298-99, 10326; Russell 10376; Thorn 11163; McNamara 11272-73; Westheimer 11438; McWilliams 11996, 11999, 12030; Howard 12894-96; Culver 12944; Hanna 13190). Sales representatives were instructed to memorize these standard presentations and follow them verbatim in all future contacts with prospective customers (Havas 9234; Dennen 9288B; Johnson 9513-15; Kolkhurst 10047-48; Kellogg 10298-99; Thorn 11163-64; McNamara 11273-74; Westheimer 11438; Gilbow 12326-27; Howard 12897; Culver 12955; Hanna 13191; Mawle 14790).

H. *Representation that Individuals Were Specially Selected for a Unique Offer*

138. Various presentations used by respondents' sales representatives conveyed the impression to individuals contacted that the offer made to them was unique and that they were specially selected or qualified to accept it. Standard presentations informed prospective customers that qualified families were being accepted or invited to participate in an unusual offer being made in their area and that if they declined to participate, their opportunity would be passed on to another family (CX 821C-E, 871G).

139. Prospective customers were informed by respondents' sales representatives that they had been selected as one of a few families in the area to receive a unique offer or to participate as a research or test family in a new program developed by respondents (Warwick 9671; Halsey 9722-23; Schneider 9898; Leach 10253, 10269, 10272; Clarke 10335-36; Ford 10560, 10573; Demer 11300-02, 11314, 11321; Bruker 12089; Clay 12429, 12435-36; Ivaska 13214). The criteria or basis on which such selection had been made, if one existed, was not, however, disclosed to prospective customers (Warwick 9685; Halsey 9723; Schneider 9915; Leach 10269, 10272; Ford 10589; Demer 11314; Bruker 12089; Ivaska 13215). [62]

140. The impression that individuals contacted had been specially selected or qualified was reinforced throughout the presentation. In addition to oral representations, retail contracts used in some sales transactions bore the designation "College Student Program" in bold red letters which reinforced the impression that participants

in the program were of a limited, select class (CX 405I, 405K, 405N, 1220A).

141. Respondents' official policy prohibited sales representatives from representing that individuals contacted had been specially selected for the program presented (RX 65A, 65B, 69A). Respondents also placed legends on contracts used by their sales representatives explicitly stating that individuals contacted had not been specially selected (RX 42–50). However, respondents were aware that, contrary to the avowed corporate policy and contract provisions, sales representatives frequently represented, directly or by implication, that the individuals contacted had been specially selected (CX 95G, 95I, 95 "O", 95M, 96D, 105H, 107D).

142. The above representations led prospective customers to believe they had been selected to participate in a program which was not available to the public at large. Such representations were false and misleading in that such individuals had not been specially selected and the program offered to them did not differ from that offered to all members of the general public on a regular basis.

I. *Representations That Certain Merchandise Was Free or at Reduced Cost*[33]

143. Respondents' official policy prohibits representations by their sales representatives to prospective customers that any publications or products included within a particular combination package are "free" or without cost, unless such representations are true (McKean 15500; see also Goldstein 14119; Stearns 14615–16). As evidence of the existence of this policy, respondents cite policy directives issued by [63] respondent Richards in 1969 (RX 65A, 69A); testimony of two consumer witnesses that they knew none of the merchandise or services they received were "free" (Lay 9760–61; Pritchard 14037); and contract language that ". . . no item listed above is free" (RX 45). Despite their announced policy, however, respondents' sales representatives made representations that publications or products included within combination packages were free, at no additional cost, or bonuses. Respondents, as a result of their 1969 telephone surveys, were aware that such misrepresentations frequently occurred (*e.g.*, CX 95E, G, I, M; 96F; 97D, F, H; 98D, F, H; 99H; 100E, K, R; 102F; 103D, H, J; 104E, G, I; 105D, F, H; 106E; 107F, I; 108F, G, J, K; 109D).

144. Once entry to a prospective customer's home was effected, most of respondents' sales representatives used a standard "advertis-

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[33] See subsection K, "Representations of Available Payment Plans—Conversion," for findings regarding representations of free merchandise for paying off contract in under ten years.

ing talk." Respondents' sales representatives stated that Grolier or one of its subsidiaries had recently developed a new product and was currently involved in a promotional campaign. After discussing the expense and lack of success of a national advertising program, prospective customers were told that respondents were embarking on a program of local "mouth-to-mouth" advertising and were seeking individuals to provide "help and cooperation" in this endeavor.[34] Under the terms of a special "help and cooperation offer," it was represented that a participating individual would receive some or all of respondents' products free or at greatly reduced costs in return for their help and cooperation in one or more of the following ways:

(1) Displaying of publications in a conspicuous location in their home;
(2) Writing a letter evaluating or endorsing the publication which may be used in future advertising;
(3) Providing respondents with referral names of individuals who might be interested in respondents' publications; and [64]
(4) Giving permission to list and use individual's name as a local owner.

(CX 419C, 446B–C, 447B, 563J, 651C, 821B–C, 997C, 1023A; Halsey 9692; Thorn 11170–71; Goldstein 14093–94; Basilici 14921, 14934–35.)

145. Respondents' sales representatives gave varying explanations to prospective customers of what they would receive for their help and cooperation. Some prospective customers were told that they would be "paid" in educational materials and services for the help and cooperation rendered by them (CX 563P, 1023A; Will 9566; Gilbow 12146, 12171–72, 12388–89). Other prospective customers were told that in exchange for their cooperation, they would be offered an opportunity to purchase respondents' products at substantial savings over the established retail prices (CX 419C, 447B, 651, 821, 997; Dennen 9281; Williams 9354–55). Standard sales presentations explained this price reduction as follows:

> . . .[I]n return for the help that we need, we'll cross all the retail price out completely (CROSS OUT PRICES). They will never apply to you. All you'll ever return to us, instead of all this, is the shipping once and the $ _____ ten times, and if you're one of the opinion poll contest winners, we'll even cross this out (CROSS OUT), in other words, you'll own the entire program free (CX 419K, 651L).

> . . . I HAVE BEEN AUTHORIZED TO DISREGARD EACH AND EVERY ONE OF THESE FIGURES I HAVE SHOWN YOU. NOT CHARGE THE FAMILY $889.80 OR

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[34] In fact, respondents' sales representatives' sole purpose in being in the home was to sell respondents' products and services (Murphy 16474).

EVEN $88.98 A YEAR BUT ACTUALLY ENROLL THE FAMILY IN THE ENTIRE 10 YEAR PROGRAM — PROVIDING THEY QUALIFY FOR LESS THAN THE COST OF A DAILY NEWSPAPER. JUST $39.95 A YEAR OR ABOUT A DIME A DAY AND MR. AND MRS. _____ THAT RIGHT THERE IS ABSOLUTELY ALL A FAMILY WOULD EVER INVEST IN THE ENTIRE 10 YEAR PROGRAM

(CX 821F.)

In other sales presentations, prospective customers were told they would pay for one or more components of the educational package but that the remaining components were bonuses or premiums given in exchange for their help and cooperation [65] (Tiburcio 8663-64; Canario 9128-31; Havas 9218 9244-45; Westheimer 11456).[38] Another variation of the "help and cooperation" theme represented that, if individuals provided such assistance, they were required only to pay to keep the program up to date for ten years via yearbooks and the Fact Research Service, but the initial program would be placed in their home without charge (CX 1023B; Will 9580-82; Warwick 9670; Halsey 9697; Nesper 9788; Schneider 9902, 9909; O'Hara 9988-89; Kolkhurst 10027; Walker 11223-24; McWilliams 12006-09, 12071-73; Clay 12431; Howard 12900; Reames 13343). Other prospective customers were told that, in addition to rendering the requested "help and cooperation," they would be required to pay only for shipping, publishing and royalties (Johnson 9522-23; Thorn 11176-77).

146. Although respondents' sales representatives were instructed not to use the word "free" in their sales presentations, euphemisms such as "premiums," "bonuses," "at no additional cost" and "at no extra charge" conveyed the impression that individuals providing help and cooperation would receive free merchandise (Tiburcio 8663-64; Canario 9128, 9131, 9149; Havas 9244-45). Offers of "free" merchandise or services which are deceptive:

> may not be corrected by the substitution of such similar words and terms as "gift," "given without charge," "bonus," or other words or terms which tend to convey the impression to the consuming public that an article of merchandise or service is "Free" (Use of the Word "Free" and Similar Representations, 16 C.F.R.251).

147. During the sales presentations, promotional materials provided by respondents to their sale representatives added credibility to oral representations that respondents were actively seeking families to cooperate in local product promotion (CX 405D-E, 406B, 406G-H, 440, 996B-C, 996F). In many instances, respondents' sales representatives used a "co-op" card containing the following

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[38] In these instances, the retail sales contract was sometimes referred to as a "receipt" which would assure that the participant was paid for the help and cooperation rendered (McWilliams 12014, 12064).

language, which purportedly set forth the obligation assumed by the customer under a help and cooperation offer: [66]

> I will cooperate with you in your local advertising program by:
>
> 1. Allowing you to refer to me as a local owner. . .
> 2. Writing a brief letter stating my opinion of your program. . .
> 3. Recommending five educationally-minded families . . .

(CX 467B.)

(See also CX 435, 467B, 974, 1024.) The representation that participants would receive educational materials in exchange for their help and cooperation was also reinforced by the "Sponsor's Guarantee" used by respondent Spencer's sales representatives which read in part:

> In return for all conditions shown above it is agreed the subscriber will:
>
> ☐ Write letter of testimony
>
> ☐ Answer questionnaire evaluating the merchandise
>
> ☐ Allow name to be used by a local owner
>
> ☐ Submit names of five prospects

(CX 812.)[36]

148. The representation that help and cooperation from participants was a condition of the transaction was also reiterated on the face of retail sales contracts used by respondents' sales representatives:

> For which I agree to cooperate by expressing my opinion of the Americana Program, by permitting you to use my name as an owner, and by recommending the names of five prospects; and for which I promise to pay to your order. . .

(CX 1222A.)

[67] (See also CX 405I, 810A, 991A, 1004A, 1095, 1226, 2046.)

149. Although help and cooperation was ostensibly sought to be used in a product promotion campaign, no such use was made of such assistance if rendered, and respondents did not attempt to verify that letters and referral names were submitted (Stearns 2657–58; Gilbow 12218; McClearey 13968; Goldstein 14162–63). Despite contract provisions, which implied that an individual's help and

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[36] This form was used before presenting customers with the retail sales contract to "ease the family into signing things" (Westheimer 11452). In some instances, the sales transaction was characterized as a "SPONSOR-OFFER based on Your Help as a Local Owner" (CX 809I).

cooperation was a condition of sale, contracts were not cancelled for failure to provide the promised assistance (Stearns 2657-58; Lay 9762; Schneider 9904; Ford 10580; Reames 13349; McClearey 13968; Basilici 14935; DeLucia 15079-80).

150. In addition to the "help and cooperation" theme, representations were made in other sales presentations that individuals would receive free merchandise for joining the Consumer Buying And Education Service and paying the contract off in three years (Geddeis 9924, 9928; Hatcher 10864, 10889; Larsen 11432-33; Krubsack 11976, 11978). As a result of such oral representations, the impression was conveyed to prospective customers that the payments they agreed to make applied only to the cost of the service and that all other merchandise received was at no additional cost (Hatcher 10864; Larsen 11411-12, 11432; Kearns 11930-31).

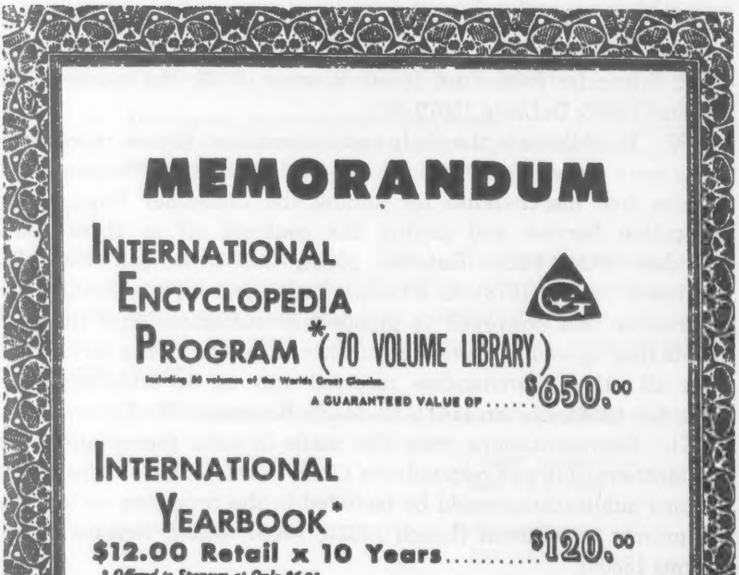
151. Representations were also made in sales presentations for the Mothers Club and respondents' Child Development Program that various publications would be included in the programs as bonuses for prompt enrollment (Leach 10255, 10257, 10284; Bricker 12095; Storms 13306).

152. Contrary to representations made by respondents' sales representations that "free" merchandise was included in the educational packages purchased, no publications or services were free (RX 45; CX 810A, 1004A, 1095A, 1222A). Such representations, therefore, were false, misleading and deceptive.

J. *Representation of Retail Prices*

153. A representation that a stated price is the list or retail price is a representation that a substantial number of sales of the article in question are made at that price (See Guides Against Deceptive Pricing, 16 C.F.R.233).

154. Respondents distribute promotional sales aids, attributing stated values to various package components, to their sales representatives for use in presenting educational packages to prospective customers. (CX 809H is one example of such memoranda: [68]



MEMORANDUM

INTERNATIONAL
ENCYCLOPEDIA
PROGRAM *(70 VOLUME LIBRARY)
Including 50 volumes of the Worlds Great Classics.
A GUARANTEED VALUE OF $650.00

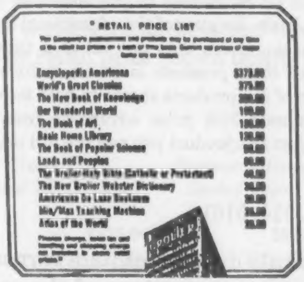
INTERNATIONAL
YEARBOOK*
$12.00 Retail x 10 Years $120.00
* *Offered to Sponsors at Only $6.95*

FACT
RESEARCH SERVICE
$35.00 Per Year* x 10 Years.... $350.00
**Based on Cost Plus Profit accounting of 10 reports*

TOTAL 10 YEAR
PROGRAM VALUE ________ $1,120.00

[69] (See also CX 831H, 973.)

155. Beginning in the late 1960's, respondents, for the stated purpose of increasing customer awareness, also began printing a price list on retail installment contracts used by their sales representatives (Murphy 16384-85). There were variations in individual item prices and format, but CX 1222B is typical of the overall impact of such retail price lists:



RETAIL PRICE LIST

Encyclopedia Americana	[illegible]
World's Great Classics	[illegible]
The New Book of Knowledge	[illegible]
Our Wonderful World	[illegible]
The Book of Art	[illegible]
Basic Home Library	[illegible]
The Book of Popular Science	[illegible]
Lands and Peoples	[illegible]
The Grolier Holy Bible (Catholic or Protestant)	[illegible]
The New Grolier Webster Dictionary	[illegible]
Americana De Luxe Bookcase	[illegible]
Min/Max Teaching Machine	[illegible]
Atlas of the World	[illegible]

(See also 420D, 810D, 1193B, 1246B; RX 509-13.).

156. The retail price lists provided by respondents were referred to by sales representatives in the course of their presentations to demonstrate the costs savings customers could realize through combination purchasing (CX 419J, 447J, 651K; Murphy 8853; Will 9579-82; Halsey 9699; McWilliams 12012; Culver 12951-52, 12958-59; Covens 13704-08; McClearey 13903-06; Goldstein 14155-58; Duvall 14866; Basilici 14932-34). The total [70] of retail prices listed contrasted sharply with the standard combination prices (Finding 168) offered to prospective customers.

157. Respondents' sales representatives were frequently not authorized to make individual sales of respondents' publications (Snyder 8759-60; Dennen 9288A; Tepker 9465; Kolkhurst 10035, 10055-56; Kellogg 10314-15; Waugh 10518-19; McWilliams 12012; Gilbow 12207-10). Other salesmen, although authorized to make individual sales, were discouraged from doing so (Culver 12958; Hanna 13205). As a result of such policies in the local offices, salesmen generally made no, or extremely rare, individual sales of respondents' publications (Havas 9223; Will 9602; Hanke 10439-40; Westheimer 11465; Latasa 11833; Gilbow 12210, 12367; Hanna 13197, 13204; Storms 13315).

158. From 1967-1971, only a small percentage of respondents' sales were comprised of individual items at the retail prices (Stearns

2663, 2650; Long 2849; Kotler 5085; Liquie 10938; Pardee 11065; Gilbow 12209; McClearey 14000; Goldstein 14161; Duvall 14899; Basilici 14924–25; DeLucia 15075–76; McKean 15565–66; Berry 15765–66; Toman 16317; Murphy 16424, 16464–65). This finding is corroborated by the insertion, in late 1973, of respondents' price advantage statement adjoining the retail price list on current contract forms. This insert reads:

> Grolier publications and products may be purchased at any time at the individual prices on a cash or time basis. Because of the educational benefits and price advantage to subscribers of purchasing more than one set at a time, *only a small fraction of Grolier's sales of any of these products is on an individual basis.* A combination purchase of two or more of the products shown in bold face automatically entitles the customer to an approximate 30% price advantage from the individual prices. If, however, you purchase just one product you pay the full price shown (emphasis added; RX 44; Toman 16298).

(See also RX 49, 50, 514, 516).

[71] 159. Respondents do not maintain corporate records enabling them to determine what percentage of the sales of their products occurred at the individual retail prices printed on retail installment contracts (CX 5N).[37]

160. The retail price lists disseminated by respondents did not correspond to the prices at which a substantial number of such publications were sold (Finding 158). The dissemination of such lists and their use by respondents' sales representatives was, therefore, false, misleading and deceptive. [72]

161. Respondents' use of retail price lists in conjunction with the combination price constitutes a direct or implied representation that the combination price is a reduction from the price at which a substantial number of sales of the articles in question have been made. The practice of making such price comparison claims without substantiating records is unfair and has the capacity to mislead.

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[37] In June 1971, at the request of the staff of the Federal Trade Commission and with the authorization of the President, General Counsel and outside counsel of Grolier, Inc., a pricing survey was undertaken to determine the percentages of individual sales of respondents' publications compared to the sales of these publications in combination (Trachtenberg 5684). CX 1518–19, a survey of the Richard's Boston office for April, October, and November 1970, which shows no individual sales of respondents' products, reflects the only compiled data generated by the pricing survey (Trachtenberg 5689). Survey forms from other fiscal offices necessary to complete the study were gathered and retained by Mr. Trachtenberg, Vice President, Director of Consumer Relations of Grolier, Inc. These forms "were discarded in late June 1972 in the course of a routine cleaning out of his files" (Respondents' Reply to Complaint Counsel's Proposed Findings of Fact and Proposed Order, p. 42; see also, Trachtenberg 240–45, 5690–92). Consequently, no final tabulation of the percentage of retail sales on an individual basis was made. Respondents maintain that "[T]his pricing study was never completed, primarily due to the fact that the Commission, in July 1971, announced the proposed complaint in this proceeding and thereby moved the proceeding from the investigation stage into the litigation phase." (Respondents' Reply, *supra*, p. 41). The failure, without persuasive justification, to preserve the basic data necessary to complete the survey warrants the inference that the survey, if completed, would not have had results significantly different from the data recorded on CX 1518–19. (See *International Union (UAW)* v. *NLRB*, 459 F.2d 1329 (D.C. Cir. 1972.)

162. Respondents' sales representatives have also used various methods to substantially build up the alleged retail value or cost of the combination offered to prospective customers in order to increase the potential savings which would result through participation in the special offers advanced. One technique to increase the retail values was through the use of inflated retail costs or values, which were either printed in the sales materials distributed to respondents' representatives or which sales representatives were trained to use in their summary of the program's value. The following chart graphically illustrates the difference between the orally stated retail prices or values and the retail price shown on the contracts:[38]

	"Retail Price" Listed on Contract	*Sales Representatives' Stated Price*	*Promotional Material's Stated Price*
Encyclopedia Americana	$375.00 (CX 470D)	$600.00 (Will 9578) $535.00 (Miller 10179)	
New Book of Knowledge	$200.00 (CX 470D)	$350.00 (Will 9645) $312.00 (Miller 10180)	
Encyclopedia International	$275.00 (CX 810D)	$419.00 (CX 821F; Westheimer 11441; Miller 12805)	$419.50 (CX 406F.)

[73] 163. Inflated retail prices were also placed on the yearbooks included within respondents' combination offers. Sales materials disseminated to representatives during their presentations cited retail prices ranging from $12.00 to $26.75 per yearbook (CX 371, 809H, 831B, 973J, 996I). Oral representations made by respondents' sales representatives to prospective customers attributed prices ranging from $34.95 to $57.80 per yearbook (Warwick 9670; Halsey 9696-97, 9715; O'Hara 9988-89; Howard 12900-01; Ivaska 13220-22; Reames 13342-43). In fact, respondents' official 1969 list price was $6.95-$7.95 per copy (CX 8D). The current yearbook list price is $7.95-$8.95 per copy (RX 45).

164. Respondents' sales representatives, in conjunction with their presentation of the retail prices of the components of the

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[38] The "Retail Price" listed on contracts in this chart refers to those prices printed on contracts used by respondents' sales representatives. During the same time period, oral representations of higher retail values than those printed on the contracts were made by sales representatives at the direction of respondents' local managers. Higher retail values were also printed on some promotional materials distributed to sales representatives by respondents for use in their presentations.

combination offered, discussed the "cost" or "liability" to the company of providing the Research or Information Service included in the package. A specific figure, *e.g.*, $3.32 per report X 100 coupons, was set forth as the cost, liability or planned retail value (CX 447I, 477A, 651K, 997E; Will 9574, 9579; Haggerty 9874-76; Schneider 9900, 9909; Miller 10181; Hanke 10465; Evans 10637; Thorn 11173-74; Walker 11222-24; Gilbow 12171, 12383; Loots 14688-89; Duvall 14886; Basilici 14933-34).

165. Sales materials prepared by respondents and used by their sales representatives also attributed specific costs or values to the Fact Research Service, *e.g.*, CX 973K:

Each request receives personal service.

Service for One Year	$75.00
(Limit to One Request per Week)	
For One Speech or Report	$10.00

Send Your Check and First Request to

RICHARDS INSTITUTE
595 Madison Avenue, New York, New York

(See also CX 428C, 485, 973K, 1023B.) In some sales promotional material, the cost of providing the Research Service was presented, and totaled with, retail prices for other components (see CX 809H, reprinted in Finding 154). The fact that the figure listed in that exhibit, $350.00 per 10 years, is footnoted "Based on Cost [74] Plus Profit accounting of 10 reports" in much smaller type, does not lessen the impact of including this figure in the "Total 10 Year Program Value" of $1,120.00. The net impression created is that the Information Service has a retail value.

166. Respondents do not sell individual research reports or the Research Service on an independent or retail basis. The Research Service can be obtained only through the purchase of one of respondents' combination offers (McDonald 5618, 5663-64). No charge is listed for the Research Service on respondents' official price list (CX 8D), and no price for the Research Service appears on the retail list printed on respondents' retail installment contracts (CX 8D).

167. The net impression created in the minds of prospective consumers by the use of cost or liability figures for the Fact Research Service in conjunction with other component figures is that the combination they receive has a substantially greater retail value with the Service. Such representation, either directly or by implica-

tion, has the capacity to mislead since there is no retail price for the Fact Research Service. The combination of cost figures for the Fact Research Service, which is not sold at retail, with retail prices or values for other products, has the capacity to mislead consumers into the belief that the total of such figures represents a combined retail value.

168. The great disparity between the represented retail value of the combination offered and the actual contract price, excluding finance and shipping charges, is apparent in the following chart:

Sales Representative	*Represented Retail Value of Combination*	*Contract Price of Combination*
Snyder	$1200-1400 (Tr. 8996)	$399.99 (Tr. 9102)
Dennen	$1600-1700 (Tr. 9312-13)	$489.50 (Tr. 9306)
Williams	$1400 (Tr. 9354)	$465.00 (Tr. 9354)
Johnson	Approx. $1300 (Tr. 9522, 9547)	Approx. $450.00 (Tr. 9522-23) [75]
Will	$1800 (Tr. 9580)	$449.50 (Tr. 9556)
O'Hara	Approx. $1100 (Tr. 9992)	Approx. $450.00 (Tr. 9989)
Kolkhurst	Approx. $1200 (Tr. 10032)	$489.50 (CX 370C; Tr. 10033)
Miller	Approx. $1000 (Tr. 10184)	Approx. $358.00 (Tr. 10194-95)
Hanke	$1260 or $1480 (Tr. 10465)	$399.99 (Tr. 10438-40)
Waugh	Approx. $2000 (Tr. 10540)	$399.50 (Tr. 10538-39)
Evans	$1000-2000 (Tr. 10729)	$399.50 (Tr. 10716)
Thorn	$1300 (Tr. 11185)	$399.50 (Tr. 11177)
Walker	$1300 (Tr. 11224)	$489.50 (CX 957A; Tr. 11225)
Westheimer	$1120 (Tr. 11457)	$399-499 (Tr. 11457)
McWilliams	Approx. $1500	$470.00

	(Tr. 12066)	(Tr. 12009)
Miller	$889.80 (Tr. 12840-41)	$449.50 (CX 810A; Tr. 12809)
Howard	$1500 (Tr. 12900)	$579.00 (Tr. 12900)
Culver	Approx. $700-800 (Tr. 12952)	$449.50 or 499.50 (Tr. 12970)
[76] *Consumers*		
Murphy	$1300 (Tr. 8853)	$499.50 (CX 1193A; Tr. 8850)
Halsey	Approx. $1100 (Tr. 9722)	$474.50 (CX 1222; Tr. 9707)
Nesper	Approx. $1000-1100 (Tr. 9794)	Approx. $300.00 (Tr. 9800)
Haggarty	Approx. $2000 (Tr. 9876)	$499.50 (CX 1220; Tr. 9869)
Laundre	Approx. $1000 (Tr. 9959-60)	$299.50 (Tr. 9958)
Ford	Approx. $1000 (Tr. 10572, 10597)	Approx. $450.00 (Tr. 10573)
Ivaska	$1400-1600 (Tr. 13225)	$489.50 (CX 1326A; Tr. 13226)
Reames	Approx. $1000 (Tr. 13347)	$489.50 CX 1341A; Tr. 13338-39)

169. Through one or more of the techniques described, *supra*, (Findings 154-67), respondents' sales representatives represented to prospective customers that they would realize substantial savings through participation in respondents' offer. In truth and in fact, the regular and usual price of respondents' products was the combination price actually paid by the consumer. [77]

K. *Representations of Available Payment Plans—Conversion*

170. In many of the sales presentations used by respondents' sales representatives, the cost of the combinations offered was presented and discussed as if prorated over a ten-year period (CX

786J, 871N-P, 1715C; Kotler 5080-81; Havas 9217; Kellogg 10311-12; McWilliams 12009-10; Miller 12842-43; Culver 12952; Hanna 13206; McClearey 13914; Goldstein 14104; Basilici 14934). The following statements from sales presentations distributed to respondents' sales representatives are illustrative of such representations:

> To make this a practical program it had to be something all families could afford. So what we did was this, we pro-rated the cost of the program over the ten years and found a family could have this entire program in their home for about the cost of a daily newspaper or $48.79 per year. . . (CX 871N-O).
>
> * * * * * * *
>
> . . . This is all sent to you for the $——— per year pro-rated over the ten years of the program. Now the $——— per year can be handled any way a family cares to handle it. This is entirely up to you. The only thing the Co. does ask is that you don't take the entire ten years to handle it since the bookkeeping costs would be enormous, and besides most families have said that a dime a day for the next ten years would get to be a nuisance, it would be like putting a mortgage on a dog house. . . (CX 871P).
>
> Conversion: Mr. & Mrs. Jones, at this point I have a bonus for you, there's no more money involved, forget money . . . You don't have to take ten years unless you want to, & of course nobody wants to. In fact the company encourages families not to because ten years of bookkeeping costs the company a fortune down in N.Y. If you will return the ten 39's to us on a systematic basis, six months, a year, two years, three years, whichever way you are most comfortable we will pay you to do it. We will send along at no extra cost, . . . Isn't [78] that amazing!! Now I prefer to set you up on the same basis I have my other families in this area, which is on the three year plan & if you want to pay it off sooner later on, you can.

(CX 1715C.)

171. The main reason respondents' sales representatives used a ten-year time frame in their presentations was that by prorating the price of a combination over that period, the impact on the consumer of the total price of a combination was lessened, *i.e.*, a "psychological cushion" was provided which minimized the shock of the total price (Havas 9262; Westheimer 11452; McClearey 13909-10, 13913).

172. Although the price of an educational program was represented as prorated over ten years, respondents' sales representatives were not authorized to offer or accept a ten-year retail installment sales contract (Snyder 8752; Havas 9222-23; 9262; Johnson 9523; O'Hara 9992; Kolkhurst 10030-31; Miller 10204; Evans 10641-42; Westheimer 11452, 11485; Latasa 11826-27; McWilliams 12011, 12070; Gilbow 12174; Miller 12807, 12842; Culver 12952).

173. The sales presentations used represented that the customer's conversion from ten years to a shorter payment period, *e.g.*, three years, would save the respondents considerable bookkeeping

expense (CX 871P, 1715C; Thorn 11177; McWilliams 12010). These savings were to be passed back to the customer in the form of premiums or bonuses of added merchandise which customers would receive "free" or at "no additional charge"[39] (CX 786J; English 528; Snyder 9005; Havas 9217-18; Will 9585-86; Halsey 9697-98, 9719; Nesper 9797; Schneider 9901; Laundre 9959; O'Hara 9991; Miller 10171; Kellogg 10312; Demer 11308; Westheimer 11449-51; Gilbow 12174, 12394-95; Miller 12808; Hanna 13197, 13210; Reames 13345).

174. By prorating over ten years the prices of combinations offered by respondents' sales representatives, either implicitly or explicitly, represented that customers could pay for such combinations over ten years if they desired (see Finding 170). In fact, the ten-year payment plan was non-existent and the "conversion" to a shorter period was illusory since a ten-year period was not, in actuality, an available alternative. Representations as to the cost of the combination prorated over ten years were, therefore, false, misleading and deceptive. [79]

L. *Representations That Program Was a One-Time Offer of Limited Duration*

175. Respondents' sales representatives were trained to impress upon prospective customers that the offer being presented to them was unique and would not be made available to them more than once (CX 786C, 871G, 871I). The Spencer Training Manual admonished sales representatives:

> DO NOT ACCEPT CALL BACKS -

(CX 871B.)

and promotional materials used by some sales representatives also stated:

> No call backs can be made, as these sets must be given out on first call basis only.

(CX 405G.)

The reason for adopting the policy against call backs was respondents' belief that if the prospect did not accept an offer the night it was presented, it was unlikely that a sale to him would ever be made (Miller 12815; Culver 12958).[40]

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[39] CX 871P states:

> ". . . using this method saves us a tremendous amount in bookkeeping. We pass that savings back to you, not in the form of a bag of loose change, but in a much nicer way, in the form of added merchandise. . . ."

176. If prospective customers requested additional time to decide whether or not to purchase the program presented, respondents' sales representative represented that he would not be in the same sales area at a later time and that the prospective customer must accept or reject the special offer made at the conclusion of the sales presentation (English 530, 548; Canario 9132–33, 9152; Warwick 9672; Halsey 9699; Geddeis 9928; Kolkhurst 10033; Waugh 10518; Westheimer 11459; Bruker 12091–92; Miller 12815; see also Miller 10190–91; Kellogg 10301; Belson 10812; Hatcher 10870; McWilliams 12016; Culver 12958; Gribbin 13128). If prospective customers had any doubts, they were asked to pass the offer up so that their program could be placed with another family in the area (CX 786C, 871G, 871J). These representations conveyed to prospective [80] customers the impression that the offer being extended was special, only available to a limited number of participants and had to be accepted immediately.

177. Respondents have no programs containing special offers which must be accepted by the customer at the time the presentation is given. At any given point in time, respondents have a single regular combination price at which such products and services are offered (CX 9–13; Trachtenberg 16188). The representation that a customer must accept an offer at the time the presentation is given because it is a special or one-time offer was false, misleading and deceptive (Goldstein 14112, 14120–21; DeLucia 15083–84, 15064).[41]

M. *Representations That Encyclopedias Offered Are "New" Editions or Publications Not Yet on the Retail Market*

178. Respondents' sales representatives frequently represented to prospective customers that the major publications offered were "new" editions or publications not yet available to the general public (CX 964C, 969A, 1023A; Murphy 8853; Will 9558–59; Warwick 9688; Schneider 9898; O'Hara 9984; Kolkhurst 10027; Walker 11257; Ivaska 13214; Reames 13340). These representations were generally integrated with the help and cooperation pitch as such representations made this approach more credible[42] (Findings 144–49).

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[40] Despite this policy, some sales representatives did, in fact, revisit prospective customers' homes on occasion if they felt they could make a sale (Westheimer 11460; Miller 12816).

[41] One of the respondents' witnesses has characterized representations of this nature as an "out and out lie" (Goldstein 14120).

[42] CX 1023A states in part: ". . . We have spent 7 1/2 years and over 4 million dollars in building and perfecting a new product, that is not yet on sale in this area . . . . Now we are setting up our local advertising in order to get local support. This is why I am here this evening. . . . the type of advertising we are interested in on a local level is letters of opinion and testimonial letters . . . ."

179. In fact, the encyclopedias referred to as "new" in the sales presentations were already on the market and available [81] to the general public at the time such representations were made.[43] These encyclopedias, moreover, had been marketed for a number of years prior to the period 1967 to 1970, to which the evidence on this point pertains.[44] Although the encyclopedias in question are subject to a continual revision policy to keep them up to date, there is, nevertheless, considerable overlap in the editorial content of these publications from one year to the next (RX 423–55). Respondents' editorial director explained their revision program as follows:

> . . . The changes are a matter of establishing priority and as far as I know, [in] no encyclopedias published by any company anywhere can everything be brought up to date every year, or else, from a financial point of view, the sets would be priced beyond the reach of virtually anyone, no it is [a] matter of priorities, and . . . it would be possible that the bulk of revision might go in a few volumes, if the most important things happened there. It might be possible some volumes would have relatively little done, but this would not be through a deliberate practice but simply because of the relative importance of the changes that were needed (Murray 16523.)

180. The representations made by respondents' sales representatives that the encyclopedias offered are new editions or publications not yet available to the general public, convey the impression to prospective customers that something more than revised editions of prior publications are offered and that such offer would not be available to all individuals seeking to purchase respondents' publications. Since these publications are neither new nor unavailable to the general public, such representations are false, misleading and deceptive. [82]

N. *The Contract, Presentations and Promotional Materials Distributed by Respondents*

181. Most of the contracts used by respondents during the period 1969 to 1971, contained the following statement:

> The publications, products and services listed above are offered at the standard combination price. This offer is not limited to any specially selected individual, group or locality and no item listed above is free (CX 810A).

(See also CX 405I; RX 43, 44, 382A, 383A, 401A, 403, 405A.) This language appeared on the face of the contract and was usually located between the payment section with the "Notice to Buyer" provision.

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[43] Although a new edition binding is used each year, the content of each such edition remains, for the most part, identical with the preceding edition.

[44] The newest of these encyclopedias, the Encyclopedia International or Collegiate Encyclopedia, was marketed for the first time in 1964 (Murray 16510–11, 16554). The Collegiate Encyclopedia is identical to the Encyclopedia International but is sold under a different binding. (*Id.*)

This statement conflicts with many of the oral representations made by respondents' sales representatives during their presentations (Findings 138-40, 144-46, 150-51, 156, 161-64, 168, 173, 176). The fact that the contract specially refutes such oral representations does not cure the original oral misrepresentations. It is unlikely that such language effectively dispels the erroneous impressions created in the consumers' mind that they were to receive merchandise or services "free" and that they had been specially selected to receive a unique offer.

182. Respondents' local offices trained their sales representatives in the method of contacting consumers and making sales presentations (Findings 136-37). These offices distributed to their sales representatives telephone talks, door approaches and sales presentations with the capacity to deceive (Findings 136-37). Promotional materials having the capacity to deceive, such as endorsement letters, were also distributed to such employees (Findings 183-94). Through such practices, respondents placed in the hands of their sales representatives the means of deception. [83]

O. *Endorsements*

183. Richards' personnel, in their sales presentations, used notebooks, known as Hot Shots, furnished to them by respondents containing among other materials various letters or pictures implying endorsement of the publications sold (Ryan 5850-52; O'Hara 9987-88; Kolkhurst 10022-24; Walker 11219). Hot Shots containing similar materials were also used by Spencer sales representatives (CX 809; Westheimer 11486; Miller 12803-04).

184. Among the promotional materials distributed by Richards to its sales personnel engaged in door-to-door selling was a picture of Pope Paul with the American Peoples Encyclopedia (CX 331E; Ryan 5853-54). Use of this picture constituted an implied representation that the publication was endorsed by the Pope. However, no permission had been granted for commerical use of the picture as this would have been contrary to the general custom of the Holy See. Pope Paul did not endorse the American Peoples Encyclopedia for commercial purposes (Powers 6143-44).[45]

185. Also included among the materials utilized by Richards is

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[45] In this connection, see also the testimony of John Ryan, President of respondent Richards:

"Q To your knowledge, has the Catholic Church or the Pope ever endorsed the American People's Encyclopedia?

A I don't think the Holy Father would endorse anything except against sin, or something like that." (Tr. 5856) the following letter signed by the President of the University of Notre Dame:[46]

> University of Notre Dame
>
> Notre Dame, Indiana
>
> Office of the President
>
> Mr. Fred W. Barend
> Office of the Manager
> American Peoples Encyclopedia
> 925 South Holman Avenue
> Chicago 7, Illinois
>
> [84] Dear Mr. Barend:
>
> On behalf of all at Notre Dame, I want to express genuine gratitude for the set of the American Peoples Encyclopedia which was recently presented to the University. We are honored and pleased to have this significant publication in our Library, and I feel sure that throughout the years the members of our teaching staff and thousands of students will find the volumes a constant source of assistance and help in their work.
>
> Please convey to all associated with you our sincere appreciation for this generous gift, and accept for yourself assurances of my warmest, personal best wishes for continued success.
>
> Cordially yours,
>
> (Rev.) Theodore M. Hesburgh, C.S.C.
> President

The circumstances surrounding the writing of this letter are as follows:[47]

1. The Notre Dame Library contains only one set of the American Peoples Encyclopedia, and this is the 1953 edition. This edition was received in late 1953 as an unsolicited gift from the publisher, Spencer;

2. The Reverend Hesburgh has looked at but never personally evaluated this encyclopedia. The letterhead appears genuine but is no longer in use. Further, it is his practice to date all correspondence and this letter, apparently written in late 1953, bears no date;

3. The Reverend Hesburgh, at the time he wrote the letter, did not intend that it would be used in [85] connection with the promotion or sale of publications to the general public and he at no

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[46] CX 379E, 1978E.

[47] The stipulation pertaining to the testimony of the President of the University of Notre Dame is dated January 1974.

time intended to authorize Grolier, Inc., Richards or any other subsidiary of Grolier, Inc. to use the letter in promotional materials relating to the sale to the general public of such publications (CX 1978A-B).

On the basis of the foregoing, it is evident that the 1953 date was removed from Reverend Hesburgh's letter prior to its utilization by respondents in their promotional materials. The letter was still being utilized by Richards' sales personnel as late as 1969-1970 (Walker 11220; Kolkhurst 10023-24).

186. Respondent Richards has used, for promotional purposes, a letter from Glenn Overman, formerly Dean of the School of Business, Oklahoma City University, under the letterhead of that University (CX 414G). Mr. Overman, while Dean of the School of Business at Oklahoma City University, received a set of the American Peoples Encyclopedia with a publication date of 1953, from one of respondents' representatives (Overman 10906). He wrote a letter to express his appreciation and evaluation of the gift in the period 1953-1956 (Overman 10908-09). It was not his intention that the letter be used as a sales aid by respondents and he never authorized Grolier, Inc. or Richards to use his name or letter for sales purposes (Overman 10909).

The letter reproduced in the Hot Shot is essentially as written by Mr. Overman. Although it is his practice to date his correspondence, it contains no date (Overman 10907-08). The date was deleted from the letter prior to its use as promotional material.[48] The only edition of the American Peoples Encyclopedia seen by Mr. Overman was the 1953 edition and his letter pertains only to that edition (Overman 10909). However, the Hot Shot containing Mr. Overman's letter was shown to prospective customers as late as 1970 (Ivaska 13218). [86]

187. The prospectus for the Encyclopedia International contains a letter used for promotional purposes by respondents written by Ernest E. McMahon, formerly Dean, University Extension Division, Rutgers University (CX 692; McMahon 9496-97). Mr. McMahon was a member of the Advisory Committee for the Encyclopedia International until some time in 1964, when he wrote this letter (Tr. 9497-98). The letter was written in response to a request from Lowell Martin, respondents' editorial director, for an evaluation of the Encyclopedia International project (McMahon 9498).

There is no date on the letter reproduced in the prospectus, although it is Mr. McMahon's practice to date his correspondence

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[48] In connection with the inference on this point, compare the stipulation concerning the testimony of Rev. Hesburgh, CX 1978.

(McMahon 9498). Mr. McMahon was not consulted concerning the deletion of the date or other alterations in his letter (Tr. 9498-99).[49] Respondents did not ask Mr. McMahon's permission to use his letter in the prospectus for promotional purposes or inform him that such use would be made of his letter (McMahon 9500). Mr. McMahon did not intend to write the letter as an endorsement of this publication (McMahon 9498). Had this been his intention, he would not have used the University letterhead (*id.*).

188. A Hot Shot utilized by Spencer contained the following representation endorsing the Fact Research Service:

Roy, Lopatin & Ward
ATTORNEYS AT LAW
2050 PENOBSCOT BLDG.
DETROIT 26, MICHIGAN

Enclosed is $10.00, please send complete report on the Tideland oil issue.

(CX 809F.)

[87] None of the members of the firm Roy, Lopatin & Ward either, individually or on behalf of the firm, has:

> (a) subscribed to, submitted questions to, paid for, or [in] any other way participated in the Grolier Fact Research Service or any other similar research service;
>
> (b) sent Grolier or any of its subsidiaries a check in the amount of ten dollars or in any amount;
>
> (c) requested or received a report on the "Tideland Oil Issue" as indicated in the first letterhead in CX 809F; or
>
> (d) authorized the use of the firm's name or letterhead for commercial or any other purposes by Grolier, Incorporated, Spencer International Press, Inc. or any of Grolier's subsidiaries or agents.

The firm members did not know that their former firm's letterhead was being used for such purposes until inquiries were made by a representative of the Federal Trade Commission in February 1971 (CX 1978C-D).

189. The same brochure also contained the following representation:

NORTH AMERICAN LIFE ASSURANCE COMPANY

10515 WEST McNICHOLS ROAD
DETROIT 21, MICHIGAN DIAMOND 1-820

THANK YOU FOR THE VERY COMPLETE AND HELPFUL REPORT, YOUR

---

[49] Some additional changes appearing in the letter as reproduced were in the salutation, the addition of some underlining, and his signature (McMahon 9499). The text of the letter is the same as in the letter Mr. McMahon sent to Mr. Martin in 1964 (Tr. 9503).

> PROMPT ATTENTION WAS CERTAINLY APPRECIATED. KEEP US ENROLLED NEXT YEAR AND BILL US AS USUAL. A CHECK FOR $10.00 IS ENCLOSED TO COVER THE LAST REPORT AND THIS SHOULD BRING OUR ACCOUNT UP TO DATE.

(CX 809F.)

However, in the case of the North American Life Assurance Company: [88]

> (a) Neither the Company nor any of its offices have had any business dealings whatsoever with Grolier Incorporated, its subsidiaries, salesmen or representatives;
>
> (b) Neither the Company nor any of its offices have ever subscribed to, paid for, requested or received reports from, participated in any way in, or endorsed the Grolier Fact Research Service or any other similar service;
>
> (c) The Company has no records of any correspondence with Grolier Incorporated or any of its subsidiaries;
>
> (d) Neither the Company nor any of its offices have ever authorized Grolier Incorporated, its subsidiaries, its salesmen or its representatives to use the Company's name or letterhead in connection with the promotion and sale of publications or services to the general public;
>
> (e) Company regulations, which bind all Company personnel and representatives, provide that no employee or representative may use the Company's name or letterhead for other than Company business, . . . [U]pon this basis the Company believes that no Company employee or representative knowingly made available to Grolier, Incorporated or to any of its subsidiaries, salesmen or agents, the Company's letterhead for use in connection with the promotion and sale of publications and services to the general public

(CX 1981A-C.)

Although the fourth letterhead printed on CX 809F is an accurate reproduction of the letterhead used at one time by the company's Detroit, Michigan branch office, the company has not carried on business at the 10515 West McNichols Road address or used that particular letterhead, since October 31, 1967 (*id.*).

190. Respondents, in their sales presentations, have used a collage of University letterheads, including such Universities as Texas, Purdue, Alabama, Boston University, Fordham, and the College of William and Mary (CX 406N). The purpose of such materials was to show that these institutions had made use of the Information Service (Sampson 2466). The following legend appears under the Fordham University letterhead: [89]

> Each report is prepared by a specialist—individually compiled, with a complete bibliography to authenticate the source of research material.[50]

Through the use of such promotional materials, respondents have represented that these Universities have used and endorsed their Information Service. Respondents have no information that any of these Universities have utilized the Information Service and they are unable to substantiate such use (Sampson 2466–67).

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[50] This material was evidently used by Hinkley in its Kansas City office (see CX 406).

191. Respondents have utilized letters and pictures implying the endorsement of their publications and services by religious figures, educators and others when the authors of such letters or the subjects of such pictures had no intention of granting permission for their use as sales promotional material. Respondents' use of such materials represents that endorsements of their publications have been made by certain individuals and organizations when, in fact, there was no bona fide endorsement.

192. Respondents have used letterheads of organizations such as law firms, universities and insurance companies to represent that they had ordered Fact Research reports when the proprietors of the letterheads had never had any business dealings with respondents. The use of such letterheads in this manner is necessarily false, misleading and deceptive.

193. Respondents have used purported endorsements where the evaluation letter in question pertained to an edition for a specific year, in connection with subsequent editions not seen or reviewed by the authors of such letters. The use of such materials is misleading for that reason alone. Representations implying endorsement of editions of the publication not seen by the authors of such letters or the subjects of such pictures are inherently deceptive.[51]

194. The use of undated testimonials or endorsements implies that they have been recently executed. Utilizing undated endorsements many years after they have been written has the capacity to mislead. [90]

P. *The Information Service*

195. The Grolier Information Service[52] is a service organization set up to provide an up-to-date supplementary source of information for the purchasers of respondents' publications. It is available to every individual who buys a major set of respondents' books (MacDonald 5618, 15616). The Service is under the direction of a Vice President of Grolier, Inc. who serves as its Director (MacDonald 5615). The Director of the Information Service reports to the Chairman of the Board of respondents' parent company (Tr. 5617).

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[51] For example, the use of Rev. Hesburgh's letter apparently continued for approximately 17 years after his courtesy letter for an unsolicited gift had been received and the date thereof excised by respondents.

[52] This Service is sometimes referred to in the record as the Fact Research Service. Sometimes, the Service is also given a name to identify it with the particular subsidiary selling the combination.

196. The Information Service provides service to all customers of Grolier's in-house subsidiaries who have purchased one of the combinations of respondents' publications (MacDonald 5618). It is available only to those customers who have purchased a combination (MacDonald 5618–19). The reports are never sold and can be secured only in exchange for a coupon (MacDonald 5653). The Service is also available to customers of companies not affiliated with respondents who purchase a package of Grolier publications (MacDonald 5618).

197. The Service handles a substantial number of inquiries. For example, the record shows the following number of requests handled in the years indicated:

1967 . . . 113,416
1968 . . . 111,415
1974 . . . 50,078

(MacDonald 15624.)

198. In 1974, the Service had 24 employees.[53] (MacDonald 5619.) This included six senior editors, six general editors and three administrative editors. The balance of the staff are clerical and production employees (MacDonald 5620). The salaries of the staff are paid by Grolier, Inc. (MacDonald 5622). The research staff must have a college degree and all of them have a master's degree. Some of the free-lance editorial employees are college professors (MacDonald 5619, 15618). [91]

The staff of the Information Service is divided into a general and a technical section. The general section deals with general knowledge categories such as English or History (MacDonald 5622). Such staff members are specialists in this subject field (MacDonald 5623).

199. The Information Service has 8,000–9,000 prepared form answers on file (MacDonald 5624). In most instances, a staff member will locate a report dealing with the subject matter identified in the subscriber's request and mail it out (MacDonald 5625).

Respondents' "Prepared Reports From the File" are also known as "Multilith Reports." They are reports researched on topics of a repetitive nature that are immediately of interest to a large portion of respondents' subscribers. They have a bibliography and generally run to about six pages of single-spaced typing. They are prepared by the Information Service staff of fulltime editors (MacDonald 15633). Usually, they run from 65 to 73 percent of the responses handled. It is respondents' goal to have as high a percentage of multilith responses as possible (MacDonald 15635). About 10 percent of the inquiries handled have been answered with "File Reports," another form of the prepared reports (MacDonald 15636).[54]

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[53] In 1968, the number was 35 (MacDonald 5619); at present, the Service has 18 employees, including 13 editors. It also retains 10 to 15 free-lance editors (MacDonald 15618–19).

The Information Service also sends out "Library Reports," which are xerox reproductions of pages from other publications (Tr. 15638). Sometimes, an additional paragraph is added to such reports to make them more responsive to an inquiry (MacDonald 15667-68).

About 4 percent of the inquiries for information in the period 1967-1976 were in the "no letters" category on the ground that the question asked was beyond the scope of the Service (MacDonald 15655). About 10 percent of the reports have been handled on an individualized basis (MacDonald 15636-37). [92]

200. The record shows the following breakdown of Information Service Reports for December 1973 and 1974, and the calendar years 1973-1974:

	December				Cumulative			
	1974		1973		1974		1973	
Inquiries Answered (Grolier Only):	#	%	#	%	#	%	#	%
Prepared Reports from File	2,239	72.1	2,422	68.7	36,408	72.7	47,737	73.7
Staff Research Answers	146	4.7	176	5.0	1,585	3.2	1,943	3.0
Answers from Ref. Libr. Sources	469	15.1	574	16.3	7,830	15.6	8,113	12.6
Inq. Refused & Spec. Corr.	151	4.9	170	4.8	2,546	5.1	3,688	5.7
Free Lance Answers	100	3.2	182	5.2	1,709	3.4	3,275	5.0
TOTAL ANSWERS (Grolier)	3,105	100.0	3,524	100.0	50,078	100.0	64,756	100.0

(RX 467.)[55]

201. Customers, after signing the contract, received the coupons for the Information Service and a brochure outlining the limitations on the Service (CX 507A-B; MacDonald 5625).

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[54] Respondents' "File Reports" are the same as "Multilith Reports" except that they are xeroxed. The only difference is one of reproduction (MacDonald 15635-36). If needed in greater quantity, a File Report will become a Multilith Report (*id.*).

[55] Staff Research Answers are individualized responses; Reference Library Sources are materials derived from the reference books in the Service's own library; and Free Lance Answers are answers prepared by outside editors (MacDonald 15632); Inq. Refused refers to the "no letters" category (see Finding 199).

202. The Information Service provides no professional advice of any kind, including subjects of a financial, legal or medical nature (MacDonald 5627). No medical advice will be given, but general information on a disease will be provided (MacDonald 5633).

The Service will not do legal research for lawyers or medical research for doctors (MacDonald 5635).[56] [93]

The Service will not supply original compositions, write speeches, or theses (MacDonald 5635). It may provide information for, but would not provide, a tailored speech (*id.*). It does not do original research and offers material from published sources only (MacDonald 15665).

203. The Information Service decides whether a request is within the scope of the service provided, and the questions not answered are generally those requesting professional advice (MacDonald 5629-30).

204. Respondents, in their sales presentations, have described the scope of the Information Service in the following terms:

> . . .THE COMPANY ACTUALLY PUTS THE *WORLDS KNOWLEDGE* AT A FAMILIES FINGERTIPS. *ANY TIME A FAMILY HAS ANY QUESTION ABOUT ANY SUBJECT UNDER THE SUN ALL THEY HAVE TO DO IS DROP A LINE TO OUR HOME OFFICE IN NEW YORK* AND IN A MATTER OF A FEW DAYS THEY'LL HAVE A COMPLETE REPORT IN THEIR LIVINGROOM. HERE'S HOW IT WORKS. . . . YOU STATE THE QUESTION, THE EXPERTS DELIVER THE ANSWERS. . . . THE GENERAL REACTION WE GET FROM MOST FAMILIES IS THAT THIS SERVICE COULD BE CONSIDERED THE MOST IMPORTANT AND VALUABLE PART OF THE ENTIRE PROGRAM. . . .
>
> NOW FOLKS, THIS SERVICE IS NOT NEW. WE HAVE SOLD IT TO BUSINESS AND PROFESSIONAL PEOPLE FOR YEARS. . . . (emphasis added; CX 821E).

> For this reason we make available a new and comprehensive method for keeping the library up-to-date which consists of much more than just a yearbook. You see, we know that all of man's knowledge cannot be contained in any one library so we enroll all our subscribers into our Research Institute. *It's a Complete question and answer service that will answer almost any question that could come into a person's mind.* . . . (emphasis added; CX 1649K).

> [94] There is only one way to keep a library like this up to date, through our INFORMATION SERVICE which actually brings your library completely up to date, up to ten times a year, and this makes up the most valuable part of your entire library. *Any problem you could have, any question you could come up with – all you do is write us and we will supply a complete and detailed report personalized for you, with your name on the cover.* EXAMPLES: Complete pre-school training programs; teaching methods and curriculum schedules for elementary, junior, and senior high schools, complete career and scholarship information; direct research on themes, termpapers, and book reports; interior decorating, home design, child care; exterior

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[56] It might, however, provide a doctor with a bibliography on a given disease (MacDonald 5635).

design and landscaping, hobbies and do-it-yourself projects (emphasis added; CX 1023B).

A broadside for the Grolier Information Service represented:

> You state your question. . .
> Experts deliver the answer

(CX 505.)

The broadside, which also contains a lengthy list of topics on which answers will be supplied, discloses no limitations on the Service.

A broadside for the Americana Information Service also contains a lengthy list of topics on which answers will be supplied under the legend "Furnishes Information and Sources of Information . . . A Storehouse of Knowledge on Practically any Subject." It discloses no limitations on the scope of the Service. In addition, this broadside contains the legend "Men — Business and Professional" (CX 661).

205. Statements such as "ANYTIME A FAMILY HAS ANY QUESTION ABOUT ANY SUBJECT UNDER THE SUN ALL THEY HAVE TO DO IS DROP A LINE TO OUR HOME OFFICE IN NEW YORK. . ." (CX 821E): "It's a Complete question and answer service that will answer almost any question that could come into a person's mind" (CX 1649L); and "You state your question . . . Experts deliver the answer" (CX 505): "Any problem you could have, any question you could come up with—all you do is write us and we will supply a complete and detailed report personalized for you, with your name [95] on the cover" (CX 1023B), represent that the Information Service will furnish answers with respect to questions on any subject.

The Research Service does not furnish answers on every subject (CX 507B). Representations to that effect are false, misleading and deceptive.

206. Certain of respondents' sales presentations containing general representations, such as "we have experts there in every field . . . anytime something new comes up and you want to know more about it right now . . . send in a letter with the coupon", were qualified with a disclosure that "we cannot supply Legal, Medical, or Investment advice" (CX 366E; see also CX 293Q).[57] Some broadsides setting forth a list of topics on which answers would be supplied did include limitations such as "exclusive business and professional research" (CX 374).

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[57] "There are three things they won't get involved with

"1. Military (National defense secrets) Detrimental to National security

"2. Medical (your own *personal* health problems)

"3. Legal (*Personal* problems or advise [sic])" (CX 293Q).

207. Certain of respondents' salesmen, in their presentation, did disclose limitations on the Information Service in that no legal or medical advice would be provided or no financial or real estate problems answered (Belson 10809; O'Hara 9990-91; Hanna 13198; Ivaska 13222; Dennen 9276). In other sales presentations, the sales representative would disclose no limitation of any kind on the service (Warwick 9685-86; Miller 10181).

208. The disclosure that no legal, medical or financial advice would be supplied did not disclose all the applicable limitations on the Information Service (see CX 507B). Such limited disclosure failed to inform the consumer, for example, that no original research would be done and that material would be furnished only from published sources (Finding 202). The complete explanation of limitations was not received by the consumer until some time after he had signed the retail installment contract. The failure to disclose all applicable limitations at the time of the sales presentation constituted the failure to disclose a material fact. [96]

209. Respondents, in their written sales promotional materials, have represented:

> [Americana Research Institute's] large research staff will compile the information individually for you *in manuscript* form.

(CX 353H.)

> Wouldn't it have been a great relief to have had authoritative help in writing your reports, reviews, speeches and in library research work while you were in college? We couldn't offer it then.
>
> But now, even with a college degree and a staff of secretaries, it will be gratifying to have our trained research workers (with the sources of all information at their disposal) prepare your speeches — digest books — give technical reports — help with problems of business or the home.
>
> Each request receives personal service

(CX 973K[58]; 1649U.)

> Each report is prepared by a specialist—individually compiled, with a complete bibliography to authenticate the source of research materials.

(CX 406N.)[59]

> The Grolier Research service works this way: You ask the questions and we find the

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[58] This language also creates the net impression that the Information Service would respond to inquiries on any subject. The broad claims inherent in material such as CX 973K are not dispelled by, and are in conflict with, the salesman's oral disclosure that medical or legal information is not provided (Dennen 9276), and the potential subscriber is not put on notice by such disclosure that professional advice generally is not available through the Information Service.

[59] This representation appeared under a reproduction of the letterhead of Fordham University.

answers. The member sends in the questions, the questions are assigned to a specialist, *the specialist prepares a personal report based on your needs.* . . .

(Emphasis supplied; CX 293Q.)

[97] 210. Through the use of statements such as "[the] research staff will compile the information individually for you" (CX 353H, 406N); and "it will be gratifying to have our trained research workers . . . prepare your speeches-digest books-give technical reports-help with problems of business or the home. Each request receives personal service," respondents have represented that the answers furnished by the Information Service are the product of detailed, exhaustive, or original research generated by the specific question asked. Such statements are false, misleading and deceptive. The Information Service does not perform original research and the great majority of replies are not answers generated by the specific question of a particular subscriber (Findings 199-200, 202).

211. Respondents' promotional material affirmatively represents that the Information Service will prepare speeches, digest books and supply technical reports (CX 973, 1649U). Respondents' salesmen, in their sales presentations, have also represented orally that the Information Service reports could be utilized for theses or term papers satisfying school requirements (Ivaska 13222-23; Larsen 11412; Belson 10809; Hatcher 10866-67; Ford 10569-70; Geddeis 9926; Nesper 9790-91, 9811-12; Warwick 9672; Thorn 11173; Miller 10180-81; Kellogg 10309-10; O'Hara 9990-91).

In addition, respondents' salesmen have been provided with sales reports having the appearance of being originally researched and of meeting requirements for term papers. One report used for such purposes was "Characteristics Of The European Tourist Industries" (CX 394A-394Z-5). This report had not, in fact, been prepared by the Information Service and is not representative of the reports provided by the Information Service (MacDonald 15691).[60]

The Information Service will not prepare speeches or reports suitable for school or college use as theses or term papers. Representations to the contrary are false, misleading and deceptive. [98]

212. Respondents, through the use of statements or phrases in their sales promotional materials such as:

> . . . [I]t will be gratifying to have our trained research workers . . . help with problems of business or the home.

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[60] This material was apparently used by the Hinkley's Kansas City office (CX 399 and 400). The printer's invoice, CX 400, documents that 300 sets of this 31-page report had been ordered by that office.

(CX 973K, 1649V.)

NOW FOLKS, THIS SERVICE IS NOT NEW. WE HAVE SOLD IT TO BUSINESS AND PROFESSIONAL PEOPLE FOR YEARS.

(CX 821E.)

. . .Any problem you could have . . . and we will supply a complete and detailed report . . . Examples: Complete pre-school training programs; teaching methods and curriculum schedules for elementary, junior, and senior high schools. . .

(CX 1023B.)

Men-Business and Professional.

(CX 661.)

have represented that the Information Service will furnish business and professional advice.

Respondents have conveyed the same representation through sales promotional materials purporting to show that universities (CX 406N) and professional people and businesses (CX 809F) have ordered the Service when in fact such institutions, persons, and firms have neither ordered nor used the Service (Findings 188-90, 192).

Respondents' salesmen, in their in-home presentations, have used materials purporting to be sample requests for information from the Research Service and responses thereto. For example, salesmen of the Americana Corporation have utilized a letter under the letterhead of a Milwaukee attorney by the name of Charles H. Gorman requesting information in the following terms:

I have an action in which applicant's condition has been diagnosed as blastomycotic osteomyelitis.

[99] Applicant was employed as a hide staker handling sheep and lamb skins that had been tanned and milled before he handled them. At no time did he handle untreated hides.

Applicant contends that his condition was caused by his occupation. I am informed that no cases have been reported in similar industries and that there is no definite relationship between the disease and the age, occupation, nativity or habitat of the patients having blastomycosis.

Have you any information that: (a) Blastomycosis or blastomycotic osteomyelitis is an occupational disease, (b) The disease is common among tannery workers?

Any information that you can give me relative to the above will be appreciated. The original hearing will be held in four days.

(CX 431A.)

Attached to this letter is a 3-page report signed by Americana Institute relating to this disease (CX 431B-D). The report, on its face, is written in scientific technical terms and references are appended.

At the bottom of the letter requesting the information, there is the following notation:

> MR. GORMAN LATER WRITES:
>
> "I appreciate your report relative to blastomycosis and osteomyelitis. The thorough information is of great value to me. I had been unsuccessful in gathering information on the subject."

(CX 431A.)

To reinforce the net impression that professional advice has been requested and received, one sales presentation stated in connection with this sample report: [100]

> Here's a rather unusual request from a law firm in Milwaukee. The lawyers had a client who had a very rare disease. The law firm was trying to sue the employer, claiming that the disease was an occupational hazard. The problem that they had, as you can see, was that the disease itself was so rare, they couldn't get enough information to take it into court. They wrote the Research Service, and we sent them back the information. . . .

(CX 292G.)

Through the use of such materials, respondents have impliedly represented that they will furnish professional advice or provide a consulting service to members of the legal profession.[61]

213. The direct or indirect representation, through statements and materials such as the foregoing, that the Information Service will provide business or professional advice or a consulting service to professionals is false, misleading and deceptive.

214. One of the limitations in the Information Service disclosed after the sale is that it "cannot guarantee to deliver answers on specific dates" (CX 507B). Reports not already prepared and requiring a personalized response may take from two weeks to a month and sometimes longer (MacDonald 15657-58). In view of respondents' emphasis on the personalized nature of the Service (Finding 209) and the value of such reports for students (Finding 210), this limitation is a material fact in evaluating the value of the Service. [101]

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[61] Certain presentations did state that "*WE DO NOT SUPPLY* LEGAL, FINANCIAL, MEDICAL, RELIGIOUS OR *THE TYPE OF ADVICE THAT WOULD BE DEEMED PROFESSIONAL*" (emphasis supplied;) (CX 439Z-4). Such disclosures do not vitiate conflicting representations in other sales presentations or promotional materials stating directly or implying that professional advice would be supplied.

V. CONTINUITY

215. In the period January 1968 to December 1971, the two primary companies involved in respondents' mail order operations were Americana Interstate and Grolier Enterprises.[62] The principal officer of the parent company responsible for coordinating the sales of the respondent mail order subsidiaries was Elsworth Howell, Vice President of Mail Order Operations (Murphy 5774; Green 1744).

216. There is, to some extent, an interrelationship between the mail order subsidiaries and the operations of the subscription book companies which sell door-to-door. The mail order subsidiaries sell supplements to encyclopedia buyers (Clarke 16676), and people who purchase publications from the home subscription subsidiaries are put on the house list of a mail order subsidiary such as Grolier Enterprises (Clarke 16678; Green 1701-02).

217. A subsidiary such as Grolier Enterprises, which sells through the mail, has three main operations: the sale of annuals or supplements to encyclopedia sets; the operation of two children's book clubs; and conducting the Mail Order Division, which includes the continuity programs of which there are about 22 (Clarke 16612).

218. Respondents' sales under their continuity programs are substantial. The shipments under respondents' continuity programs for the period 1970 to 1975 are summarized as follows:

CONTINUITY SHIPMENTS 1970 - 1975

YEAR	*NEW ORDERS*	*SINGLE SHIPMENTS*	*BULK SHIPMENTS*	*TOTAL SHIPMENTS*	*TOTAL BOOKS SHIPPED*
1970	398,253	734,997	108,081	1,241,331	2,754,465
1971	1,017,749	2,417,168	200,816	3,635,733	6,647,973
1972	1,741,913	3,502,836	286,267	5,531,016	10,111,288
1973	1,667,742	1,596,499	282,116	3,546,357	8,060,213
1974	717,935	1,754,849	197,846	2,670,630	5,836,166
1975(EST)	735,000	1,027,000	172,000	1,934,000	4,686,000
TOTAL	6,278,592	11,033,349	1,247,126	18,559,067	38,096,105

(RX 548)

[102] 219. Continuity orders may be generated by direct mailing, solicitation, or space advertising (Clarke 16645). And, the language of the promotional materials used by the Grolier subsidiary mail

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[62] In 1969, the same individual, Howard Green, became Chairman of the Board of Americana Interstate and Grolier Enterprises, as well as certain other Grolier mail order subsidiaries (Green 1683-86).

order companies in their continuity programs is generally the same when they utilize the same programs (Green 1703–04).

220. A continuity book program generally involves the sale, on a trial basis, of a series of books ranging from 4 through 20 volumes in a particular subject area. Under such programs, the first volume is generally offered free or on trial; volumes 2 and 3 are shipped singly at intervals; and, if a cancellation has not been received, the balance of the set, usually 17 to 20 volumes, is then shipped to the customer in one shipment (Clarke 16612–13).

The shipping schedule and interval between the shipments under a continuity program may vary. At one point, the interval between shipments was monthly, then respondents went to a 6-week interval and, more recently, the shipments have been at 5-week intervals (Clarke 16613). The interval between shipments for the continuity programs in the period 1965 to 1970 was 4 to 5 weeks (Clarke 16618).[63]

221. Since March 1, 1971, with two exceptions, respondents' initial mailings have explicitly disclosed that the customer would receive a bulk shipment of books after receipt of their third volume (Clarke 16622–23). In the period 1965 to 1970, the mailings or advertisements constituting the initial contact with the customer did not, however, contain this disclosure (Clarke 16667). In that period, such notice was sent out with the third volume in the series (Clarke 16681).

222. Prior to 1971, a typical initial mailing pertaining to a continuity program contained, in pertinent part, the following representations:

Here's a free animal book for your favorite 7 to 9 year old.

(CX 1385A.)

[103] I have affixed my FREE GIFT STAMP at right. Please send me the introductory volume, ANIMALS DO THE STRANGEST THINGS, to keep forever without cost or obligation. I will then be entitled to receive new Step Up selections, on approval, which I may keep for the subscriber's special price of only $1.65 each, plus small mailing charge, or return to you in 7 days at your expense and owe nothing.

I understand I may cancel my subscription to the STEP-UP PROGRAM at any time, and you will send no more volumes after receiving my notice of cancellation.

(CX 1385B.)[64]

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[63] The shipments were on a monthly cycle in 1969 and part of 1970, according to another of respondents' officials (Green 1713).

[64] The CX 1385 and 1386 series, pertaining to Grolier Enterprises' Step-Up book program and featuring as a free volume *Animals Do The Strangest Things*, were mailed to consumers in 1969 (Allen 9937–41).

This mailing also represented that the free volume "is yours with no strings attached" (CX 1385D), *"Accept your free book today. There's no obligation!"* (CX 1385F), and represented in addition:

> But what if you're not completely sold on the program after receiving your free book? Well, in that case just write "cancel" across the membership card we'll send you, mail it to us, and keep the book as our gift. There'll be nothing to pay, and we'll simply forget the matter.
>
> * * * * * * *
>
> Nothing could be safer than the offer I'm making to you. The delightful *Animals Do the Strangest Things* is yours to keep no matter what, and you'll be under no obligation to receive any additional STEP-UP BOOKS.

(CX 1385G.)

223. An enclosure with the free volume made the following representation: [104]

> If you and your youngster would like to have more STEP-UP BOOKS, you'll be entitled to receive — on approval — as many selections as you like for the low price of $1.65 each, plus delivery.

(CX 1386A.)

> As a member of the STEP-UP BOOK PROGRAM, you are not obligated to take any minimum number of books. Accept as many or as few as you please, and cancel your membership whenever you like by mailing any invoice back to me with "CANCEL" written across it.

(CX 1386B.)

224. A "Dear Parent" letter enclosed with the third volume in the series disclosed that a bulk shipment would be sent in the following terms:

> . . .[We] have made special arrangements that will enable our good customers to receive all 15 remaining volumes in the STEP-UP LIBRARY, on approval, in one big exciting shipment!

(CX 1386C.)

> But in case you prefer that your child continue to receive his books on a monthly basis, please write to me promptly. We'll wait thirty days before sending the complete STEP-UP LIBRARY to your home.
>
> Please remember though, regardless of how you receive them — in one exciting shipment or, one at a time — your Step-Up Books come to you on trial. You may keep as many or as few as you choose.

(CX 1386D.)

225. The letter to the consumer enclosed with the bulk shipment made the following representation:

> *Please remember this added advantage:* although your child has full use of all the volumes in the STEP-UP LIBRARY *now,* you may continue to pay at the same low, volume-a-month rate as before.

(CX 1386E.)

[105] 226. The representations contained in the Americana Interstate mailings pertaining to the Step-Up Program, a continuity program also distributed by that respondent, were essentially the same as those disseminated by Grolier Enterprises (Findings 222-25). For example, Americana Interstate's initial mailing offering the free volume, *Animals Do the Strangest Things,* contains certain representations identical to, or essentially the same as, those in the Grolier Enterprise mailings (Compare CX 1383B with CX 1385B). It too represents:

> . . . Please send me the introductory volume . . . to keep forever without cost or obligation. I will then be entitled to receive new Step Up selections, on approval, which I may keep for the subscriber's special price of only $1.65 each . . . or return to you in 7 days at your expense and owe nothing.
>
> I understand I may cancel my subscription to the STEP-UP PROGRAM at any time, and you will send no more volumes after receiving my notice of cancellation.

(CX 1383B.)

The "Dear Parent" letter in the initial mailing states:

> When the book arrives, turn it over to your child and watch his reaction. If he's as pleased as I think he'll be, fine and dandy. You'll then be entitled to receive as many (or as few) additional STEP-UP BOOKS as you please, for the modest price of $1.65 each, plus delivery. Books will be sent to you on approval, and you'll have 10 days to decide whether to keep a book or return it at my expense.

(CX 1383G.)

That letter also states that the free book "is yours with no strings attached" (CX 1383E).

227. The letter enclosed with the free book states: [106]

> If you and your youngster would like to have more STEP-UP BOOKS, you'll be entitled to receive — on approval — as many selections as you like for the low price of $1.65 each, plus delivery.
>
> As a member of the STEP-UP BOOK PROGRAM, you are not obligated to take any minimum number of books. Accept as many or as few as you please, and cancel your

membership whenever you like by mailing any invoice back to me with "CANCEL" written across it.

(CX 1384A & B.)

228. The letter enclosed with the third volume gives the following notice of the bulk shipment stating:

***But now for the good news I promised you!* Thanks to special arrangements we have made, we are happy to tell you that if your remittance has been received by us within the next 30 days, the remaining 15 volumes of the STEP-UP LIBRARY can be sent in your next shipment!**

This means your little ones may have the complete 18-volume set NOW rather than waiting over a year to accumulate all volumes. But that's just PART of the good news . . . here's the rest:

This credit is extended *at no added charge*

and

Your monthly payments remain *exactly the same!*

Yes, in about a month, if your account is up to date, you should receive the balance of the set (volumes 4 through 18) in one single postage paid package. And remember, you may continue to pay for each book at the same low volume-a-month rate as before! That's just *$1.65 per month* plus shipping and handling! [107]

There's no large sum to pay and no increased payments. Your child gets the benefits of full possession now, without altering your easy monthly payment schedule by even a penny!

> **However, if for any reason you do not wish all of these wonderful volumes delivered together, please write us promptly and we'll continue to ship on a monthly basis. We'll wait 30 days before we ship the rest of your STEP-UP LIBRARY books.**

(CX 1384C.)

Yes, when the rest of your child's Step-Up Books arrive in a few weeks — on approval, of course — I'm confident you'll find them a unique contribution to your youngster's education.

But in case you prefer that your child continue to receive his books on a monthly basis, please write to me promptly. We'll wait 30 days before sending the full STEP-UP LIBRARY to your home.

Also remember, the remaining Step-Up Books will come to you on trial. You may keep as many or as few of them as you wish! In any event, you have 7 full days to examine the books without obligation of any kind.

(CX 1384E.)[65]

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[65] The letter enclosed with the bulk shipment states the following:

(Continued)

[108] 229. In the case of the Audubon Nature Encyclopedia, a continuity program distributed by Grolier Enterprises, the letter accompanying the free volume of that series stated:

> Your free first volume entitles you and your family to see future volumes of the Encyclopedia as they are released — at the rate of about one a month — for 10 days free examination. You may take as many or as few volumes as you wish, and cancel whenever you wish. In any case, Volume I is yours to keep free."

(CX 1398A-B.)

The customer subscribing to that program was, however, advised in the letter accompanying the third volume that he would be sent, on approval, the remaining volumes of the set in one shipment (CX 1398C).[66]

230. The foregoing and other of respondents' promotional materials[67] in the record constituting the initial contact with the consumer conveyed the net impression that the books offered under respondents' continuity programs are to be shipped singly with the consumers having the opportunity to review and approve or reject the individual volumes shipped in that manner and that the program could be cancelled at any time. This finding is made upon the basis of a reading of the materials in question. (See also Allen 9939; Patzke 10065; Larcey 10135; Ray 10237; Stipulation of testimony re Mrs. Barbara Gilkinson contained in CX 1985; Hutton 10484; Fuller 11338; Bjerke 12682-83; Hudgins 12721; Hankinson 12747; Schmidt 12861.) Such representations are misleading since, in fact, customers are subject to receiving a bulk shipment if they do not successfully exercise the negative option provided. [109]

231. The customer's understanding that single books would be shipped monthly and that the books could be accepted or rejected on an individual basis was an important factor in the decision to participate in the continuity programs (*e.g.*, Larcey 10135; Ray 10236-37; Skwarlo 10400-01; Hudgins 12730-31). The failure to advise consumers on the first contact that they would, after the third

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"*Please remember this added advantage!* Even though your youngster has received all of these books at once, you may continue to pay for them at the *same low volume-a-month rate as before.*

"You will note that the enclosed invoice is for Volume 4 *only.* This way, your youngster has the complete 18-volume set NOW - rather than waiting more than a year to accumulate all 18 books - yet your monthly payment of $1.65, plus shipping and handling, has remained exactly the same! What's more . . . *there's no charge for this credit!*" (CX 1384G.)

[66] This letter also advises that the subscriber can continue to pay for the books at the rate of $3.98 a month; that, if he does not wish to receive the bulk shipment, he should advise respondent promptly so that he would continue to receive the books on a monthly basis. The letter also represents that respondent would wait 30 days to ship the rest of the set (CX 1398C & E).

[67] *E.g.*, CX 1387-8 (Dandelion Library); CX 1486-7 (Dandelion Library); CX 1468 (Step-Up Books); CX 1389 (Companion Library); CX 1375 (Illustrated Encyclopedia of the Animal Kingdom).

volume, receive a mass or bulk shipment of the remaining volumes constituted the failure to disclose a material fact.[68]

232. It was respondents' policy to continue single shipments of books if the customer, subsequent to receiving notice of the bulk shipment, requested the continuance of shipments on an individual basis and if such request was received prior to mailing of the bulk shipment (Clarke 16681-82). However, if the letter requesting single shipments was delayed or, if there was a delay in respondents' processing of such request prior to sending out the bulk shipment, the customer would not continue to receive the volumes on an individual basis (Tr. 16682).

The record shows that certain customers who advised respondents that they did not want the bulk shipment, but did desire to continue receiving the books on a monthly basis, were not given that opportunity (Allen 9942-44).

233. Once the bulk shipment is received, the consumer does not have a realistic opportunity to accept or reject particular volumes. Less than 1 percent of the consumers receiving a bulk shipment made a choice between the books contained in such a shipment in determining whether to retain or return particular books (Clarke 16690).

234. As already noted, respondents' promotional materials repeatedly represented that customers incur no risks or obligations in embarking on the continuity programs (Findings 222-23, 226-27, 229-30). Subscribers to respondents' continuity programs are, however, subject to various risks and obligations if they decide to participate in such a program. The first and most obvious, if they do not desire certain books, is the duty to exercise [110] their negative option to notify respondents of that fact, particularly in the case of the bulk shipment (Finding 232). In addition, they have the obligation of returning the books rejected.

235. The customer, if he exercises the negative option to reject additional books, is also, as a practical matter, subject to certain additional risks. For example, if a subscriber cancels his account by means of rejecting the publication and there is a delay in respondents' receipt of the returned books, this triggers either the next shipment or a dunning letter (Clarke 16692). Moreover, respondents may experience delays in sending out books or delays in taking care of cancellations. Such occurrences are not uncommon even though they may constitute a small number of the transactions involved (Clarke 16694-95). The number of such occurrences was, in

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[68] A number of the consumers testifying herein preferred monthly shipments because their children looked forward to getting the books in the mail (Ray 10236; Bjerke 12683-84).

fact, substantial. In the period 1965 to 1970, 8 to 12 percent of the correspondence received indicated that there had been crossing in the mail between the delivery of the books and the sending out of a cancellation (Clarke 16701-02).

Certain of the customers who participated in one of respondents' continuity programs on the understanding that books would be shipped singly on a monthly basis, promptly exercised their negative option to advise respondents that they did not want a bulk shipment. Nevertheless, they were mailed the bulk shipment they did not want, and were then obligated to return such books (Allen 9942; Patzke 10067-68; Larcey 10137-39; Hudgins 12723). Moreover, some customers who received the unwanted shipment and returned it were subjected in certain instances to a lengthy series of dunning letters[69] and the necessity of corresponding with respondents, at times unsuccessfully, to straighten the situation out (CX 1464A-C; Skwarlo 10394-95; Bjerke 12687; Hudgins 12724-25, 12738-39; Hankinson 12749-50; Patzke 10068-69).

236. The representation that those who participate in such continuity programs do so at no risk or obligation is deceptive. [111]

VI. DEBT COLLECTION PRACTICES

237. Beginning in the mid-1960's, Grolier, Inc. attempted to consolidate the credit and collection activities of its direct selling subsidiaries in Federated Credit (Walker 5931-32; Murphy 5739). Such consolidation, however, was not complete. Certain officers of the respondent's direct selling subsidiaries continued their own collection efforts (Walker 5936-37).

Richards collected its own accounts through a network of branch and regional offices and its headquarters in New York (Ball 2929-30; Liquie 10923; Smith 4368; Ryan 5809, 5819). Richards, in its debt collection procedures, attempted to adhere to the policies of its parent, Grolier, Inc. (Ryan 5809).

The mail order subsidiaries, such as Americana Interstate, Career Institute and Grolier Enterprises, have engaged in their own collection efforts utilizing dunning forms mailed directly to their subscribers (Green 1734-39, 1741).

238. Respondents, in their debt collection procedures, utilized a

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[69] Respondents' dunning letters in connection with the continuity programs usually go out on a 30-day cycle once they begin (Green 1717; CX 1423A-M; CX 2551(a)-255Z-4). Such series ran the gamut from notices stating essentially that an account was past due to letters threatening that delinquent accounts would be reported to a credit index (CX 1423B, K; 1425), and threats such as "your name must appear on my 'delinquent customer' ", and "your credit rating is valuable and I know you will want to protect your good name by making payment promptly" (CX 255R). The CX 255 series pertains to Americana Interstate, while the CX 1423 series are forms utilized by Grolier Enterprises. (See also Section VI.)

billing sequence schedule whereunder a series of form letters, numbering 10, 15 or 20, would be sent out to customers. Normally, the sequence would start 10 to 15 days after a debt first became past due. If the debt remained unpaid, the letters and notices sent out would be varied. Every 10 days or each week, the customer would receive a different letter (Dierking 2335-36; see also Ryan 5819; Smith 4373; CX 163A).

239. The forms in a typical collection series utilized by Federated Credit, such as CX 151A-151-Z-15, run the gamut from past due notices, stating that payment would be appreciated, to threats that adverse credit reports would issue and that the accounts would be turned over to an attorney, as well as form letters under an attorney's letterhead threatening to institute suit (CX 151B, 151S, 151J, 151-Z-11).

240. Federated Credit has utilized debt collection letters represented as coming from the "Legal Department." For example, respondent has sent out notices as follows: [112]

LEGAL DEPARTMENT

> Indicate the name and telephone number of your attorney on the bottom of this letter and return it to us. Your account has been referred to this department for suit and this information will make it easier for this department and your attorney to get together on the matter.
>
> However, if you plan to handle the matter yourself, just make out your check for the full balance due and mail it to us.
>
> BALANCE ______________
>
> Sincerely,
>
> Legal Department

(CX 157G.)

(See also CX 157C, D, E; CX 280R, S, U, V, Z-4, Z-7, Z-8.)

241. The Federated Credit office in Los Angeles, in the period 1969-1970, operated a unit described as a "Legal Department" (Mercier 14742-43). It consisted of one clerical employee with no legal training, who acted as a liaison with an outside attorney handling collections for Federated Credit (Mercier 14763-65). This employee would sign the attorney's name to the stationery bearing an attorney's letterhead but with the address and telephone number of Federated Credit (Mercier 14763-65; CX 280Z-280-Z-2).[70] Tele-

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[70] The decision to send the attorney letters would be made within Federated Credit and the outside attorney would not become involved unless there was a decision to sue (Mercier 14764).

phone calls generated by such attorney letters would be handled by the employee in the Legal Department who would try to adjust the account (Mercier 14764-65). This unit in the Los Angeles Federated Credit office had no one employed therein with [113] legal training (Mercier 14742-43, 14764-65).[71] The operation was not a bona fide Legal Department.

242. Richards also used forms representing that a customer's account had been transferred to its Legal Department (CX 177M).

243. Richards and the local offices of the respondent subsidiaries engaged in collection had no Legal Department (Ryan 5819; Dierking 2342-43; Cooney 2570). The use of this terminology on such collection forms is false, misleading and deceptive.

244. Respondents' typical fiscal office did routine credit verifications prior to acceptance of an order, and conducted collection efforts once the account became delinquent (Mercier 14728). Once an account was verified and accepted, a predetermined billing and collection schedule would be used to handle the account (Bodkin 2578; Smith 4374; Mercier 14759-60, *e.g.,* dunning schedules CX 150A-B, 280Z-20, 1825-26). Clerical personnel select the appropriate dunning letter, depending on the stage of delinquency, and mail it to the alleged delinquent debtor (Mercier 14728, 14759-60). The difference between the credit and collection departments would be the extent of the delinquency of the account; the credit department handled accounts which were from 30 to 90 days delinquent and the collection department handled accounts which were from 120 days to 12 months delinquent (Mercier 14728). Often, the clerical personnel of both departments occupied space in a large room with different persons assigned to handle accounts in prescribed stages of delinquency (Mercier 14728, 14730, 14761). The files of the delinquent debtors are physically transferred automatically from credit personnel at the point of 90 days' delinquency to collection personnel who continue the attempted collection of the accounts (Mercier 14728, 14760-61). The mere fact that accounts were transferred from the credit department to [114] the collection department on a predetermined schedule will not sustain a finding that respondents did not have separate collection and credit departments.

245. Respondents routinely use forms representing that a delinquent account will be turned over to attorneys for collection (*e.g.,* RX 329T, 151Q, 151Z-3, 151Z-13). Such forms are followed by other forms in the same collection series going out under a lawyer's

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[71] The Legal Department in the person of a clerical employee also had instructions to phone "to Personnel Dept. at subscriber's job. Represent ourself as attorney's office advising them of subscriber's delinquency. Call is very courteous and friendly and interested in resolving problem without running an attachment which could result in extra work for them" (CX 280E).

letterhead, the so-called "attorney letters" (see *infra, e.g.,* RX 330A–F; CX 151Z–11, 151Z–14–151Z–15).

246. Federated Credit's Bethesda, Maryland office used the letterhead of a Maryland attorney on certain of its collection forms in the period 1966–1970 (Tr. 9314–15). This attorney reviewed, with one exception, the forms which were to be used in connection with his name. This lawyer and respondents agreed that his name, but not his telephone number or address, were to be used in the letterhead of the collection forms going out under his name.[72] He never signed such letters or saw such forms with the name of a debtor thereon (Tr. 9321–22); the files of delinquent debtors were not sent to him (Tr. 9322); he never asked for authority to file suit (Tr. 9323); and it was understood that he would not review responses to form letters sent under his name (Tr. 9329). In return for permitting such use of his name and signature, he received compensation of $20 a month (Tr. 9332).

Letters going out under his name stated in pertinent part:

> The Division Manager of Federated Credit Corporation has consulted me relative to your delinquent account and has instructed me to take action to protect his company's interests (CX 151Z–10).
>
> * * * * * *
>
> This morning I received a telephone call from the Manager of Federated Credit Corporation, informing me that you still have not paid on your account. [115]
>
> He requested that I immediately re-open this case and file suit in a local court to obtain a judgment against you for the full balance due on your account plus all court costs. In order to protect my client's interests, I am proceeding with this preparation of the necessary papers.
>
> Despite the fact that this is the second time my client has found it necessary to have me act on this claim, I am writing to you to give you a final opportunity to make payment on this account.
>
> Unless I hear from Federated Credit Corporation, that you have gotten in touch with them and made satisfactory arrangements for taking care of this account, I shall proceed as my client has directed.
>
> Yours very truly,
>
> Attorney at Law

(CX 151Z–14.)

247. In the period 1971 to March 1974, the Kansas City office of

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[72] There was an interval from late 1968 to 1969 when such agreement was not in effect (Tr. 9315).

Federated Credit used various forms threatening delinquent accounts with suit (*e.g.*, CX 1829Z-54, 1829Z-58; Cooney 2569).[73] This office, in the same period, also used collection forms under the letterhead of a local law firm (CX 1829Z-63-67). These attorney letters impliedly represent that suit would be filed against debtors failing to make payments.[74] Such forms were to be used for those accounts that were in "extreme arrears," namely, [116] at least six months' consecutive delinquency and eight months' contractual delinquency. The determination whether to send out the letters under the law firm's letterhead was made by the Fiscal Administrator for Federated Credit's Kansas City office or his collection supervisors. The form letters, but not the files of the customers, were sent to the law firm before the forms were mailed. This law firm has filed no suits in behalf of Federated Credit (Cooney 2571-72).[75]

248. In 1970, the Los Angeles office of Federated Credit received instructions from the New York office that all legal action was to be discontinued. Pursuant to those instructions, no lawsuits were filed by that office from mid-1970 through 1975 (Mercier 14734-35).

249. Beginning in 1972, the Los Angeles Federated Credit office began using collection letters under the letterhead of a local attorney (Mercier 14752). The letters were approved by Federated Credit's head office in New York (Tr. 14753-54). One of these letters indicated that the lawyer had been requested by Federated Credit "if necessary, [to] take the proper steps to collect this debt" (RX 330A). Another of these letters stated:

> I have afforded you every possible opportunity to make arrangements for satisfactory payment on your delinquent account with Federated Credit Corporation, but you have not responded.
>
> Federated Credit Corporation has instructed me to proceed with forceful collection of your account for the entire outstanding balance. I will not continue the expensive procedure of writing to you. If you do not send the entire balance due by return mail, I shall have no alternative but to proceed per their instructions.

(RX 330E.)

[117] Such letters impliedly represent that suit will be filed or other legal process instituted if a satisfactory reply is not received.

Federated Credit's collectors determined when to send such letters. The letters would be sent to this attorney for signature along with certain records (Tr. 14754-55). Fifty to 300 letters under this letterhead could be sent in a month (Tr. 14755). The attorney, in return, received 50 cents a letter, postage and nothing else (Tr. 14755-56). These letters were sent out after the policy to stop filing suits had been put into effect (Tr. 14752). They were used because of their impact on the debtor (Mercier 14757-58).

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[73] "Legal action on your account can be postponed only if you forward a substantial payment at once" (CX 1829Z-58).

[74] "Federated Credit Corporation has instructed me to proceed with forceful collection of your account for the entire outstanding balance. I will not continue the expensive procedure of writing to you. If you do not send the entire balance due by return mail, I shall have no alternative but to proceed per their instructions" (CX 1829Z-66).

[75] The record is unclear in this instance whether the actual mailing was done by Federated Credit's personnel or that of the law firm (Cooney 2571).

250. In 1965, Richards entered into an agreement with a John Doe, Esq.,[76] of the Illinois Bar, which provided that Richards would be permitted to use his name on collection letters prepared by Richards in connection with the collection of delinquent accounts. This attorney initially approved the format of such collection letters. He never personally prepared or mailed such letters to customers of Richards for the purpose of collecting delinquent accounts. Pursuant to such agreement, this attorney was compensated by Richards in the period 1965 to 1969, and such forms utilizing his letterhead were mailed to delinquent debtors of Richards in that period.

The address and telephone number printed under John Doe's name in the letterhead of these forms were, at the time of the agreement, the address and telephone number of Richards. John Doe maintained no office and shared no space in that location.

John Doe never instituted, nor did he intend to institute, any legal action or suit on behalf of Richards at any time (CX 1982).

The letters in question threatened the delinquent account with legal action if no payment was made or reply received. One of the John Doe letters represented the following:

> Dear Mr.
>
> The Richards Company, Inc., has placed in my hands for immediate collection a claim against you for $ ———, being the balance due from you on a legally binding contract made by you with my client.
>
> It is hardly necessary to call your attention to the fact that the courts offer ample means for enforcing collection of moneys due under such contracts.
>
> Will you mail the account indicated to me at once and thus make it unnecessary for me to institute a court action for its collection?
>
> Very truly yours,
>
> Attorney - at - Law

(CX 268.)

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[76] His testimony was stipulated, the parties agreeing that his identity is not material to the allegations of the complaint (CX 1982A).

(See also CX 267, 269A, 270A, 271A.)

John Doe terminated the agreement with Richards on November 24, 1970 (CX 1982B).

251. Richards also used attorney letters in the Los Angeles area pursuant to an agreement with a member of the California Bar commencing in 1966, and continuing for approximately four years (Tr. 11765, 11757). This attorney was shown four collection letters by a Richards' official and it was agreed that his name would be used in the letterhead, but that Richards' address and telephone number would be utilized (Tr. 11767, 11769). The arrangement between Richards and this attorney also provided that someone else would sign his name (Tr. 11767). Richards never sent this attorney any delinquent accounts, and he did not know which [119] customers would be sent such collection letters (Tr. 11771).[77] This lawyer had only one discussion with anyone at Richards concerning accounts to whom such letters had been sent, and this involved the friend of an acquaintance (Tr. 11772). He brought no lawsuits on behalf of Richards (Tr. 11772).[78] The letters sent out under his name directly or impliedly threatened legal action. For example:

> As my recent letter regarding your long past due account with The Richards Company, Inc., has brought no reply, I hereby advise you that on ———, ——————, I intend to institute court proceedings to recover the amount of $———, plus all legal expenses.
>
> Very truly yours,
>
> File #
> A-D

(CX 178I.)
(See also CX 178F-H.)

252. Similar letters were sent from Richards' Kansas City office in the period 1965-1974 (Liquie 10934). These letters, utilizing the letterhead of a Kansas City attorney, were mailed out by the Richards office and signed by Richards' billing clerk who usually initialled the letters (Tr. 10934-35). The address utilized on these forms was that of [120] Richards (Tr. 10935). Initially, this attorney received a list of the account numbers and the subscribers' names. After some time, this became too bothersome and was discontinued

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[77] "They just said that they would pick out accounts that had not paid and would be sending them out, because it would be all too inconvenient to send over the accounts to my office and to review it and send them back to the Richards Company. So they said they would just be sending out the letters to those accounts which were delinquent" (Tr. 11771).

[78] Originally, there was some discussion that suits might be filed but none were ever sent to his office (Tr. 11172-73).

(Tr. 10935). During the relevant period, this lawyer never brought suits on behalf of Richards to collect delinquent accounts nor was he ever authorized to bring suits during that time (Tr. 10935-36). The letters going out under his letterhead and signature also threatened legal action if respondents' claims were not met (CX 198-200).

253. Richards also, as part of its billing cycle, has sent out collection forms threatening delinquent accounts with suit in the following terms:

FINAL NOTICE is hereby given this day of ——

THAT, unless your delinquent account in the amount of $ —— is paid within five days from the date hereof, our attorney will proceed with immediate court action.

THAT you may be liable for interest at the legal rate for the period of delinquency of the above stated account and all costs incident to court action.

THIS NOTICE is sent so that you will have full knowledge of the intended action.

THE RICHARDS COMPANY INC.

(CX 172, 175H.)

254. Richards utilized forms having the appearance of a legal document representing that court action would be filed. For example:

THE RICHARDS CO., INC.
Creditor File No. ____________
vs
Amount Due, $ ______
____
Debtor

[121] NOTICE TO ______________________ DEBTOR:

Repeated demands for payment of this obligation have been Ignored; THEREFORE, YOU are hereby notified that unless settlement is made within five days from date, legal proceedings will be instituted to recover this claim in full together with attorney fees, court costs, and such other relief as the court may deem proper.

THE RICHARDS CO., INC.
Creditor

Dated ______________ this ______ day of ______, 19______

(CX 188; see also CX 189, 176W.)

255. The basic policy of Grolier, Inc., which has been of long

standing, is not to sue delinquent accounts, and the filing of suit is an exception to the general policy (Murphy 16471-73).[79]

256. Respondents' use of collection forms under attorney letterheads has represented, contrary to fact, that the attorney in question has prepared and originated such letters when he did not (Findings 246, 249-51).

257. Respondents' use of letters with the letterheads of attorneys who perform no legal work in connection with such accounts represent, contrary to fact, that the account has been turned over to that lawyer for collection (Findings 246-47, 249-51).

258. Respondents' use of attorney letters as a collection device has represented directly or indirectly, contrary to fact, that suit would be filed or legal steps taken by the lawyer named in such forms when in fact he had no authority to take such steps and no decision had been made as to whether [122] such steps would be taken at the time the form was mailed[80] (Findings 246-47, 249-52).

259. The use of forms simulating or depicting legal process, at a time when no decision to institute such steps had been taken, also had the capacity to deceive.

260. Federated Credit has disseminated notices to debtors indicating that they would be subject to having adverse credit reports disseminated absent a payment within a certain period. In this connection, Federated Credit has sent out notices under the letterhead of Merchants' Credit Guide Co. stating as follows: [123]

> This company compiles information and issues reports concerning the manner in which individuals pay their just obligations.
>
> * * * * * * *
>
> We never issue a report without first giving the debtor an opportunity to pay the account, or to offer a reasonable explanation why payment should not be made as

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[79] "We do not think it is in the best interest of this company to have a massive amount of lawsuits going on around the world or in the country" (Murphy 16472).

[80] The record shows that suspense accounts, namely, those where no payments had been made for nine months, were transferred from local branches to Federated Credit's New York office (Haber 16142F, G). This office would make the decision whether to send such accounts to outside attorneys or collection agencies for collection (Haber 16142L). The Grolier employee in charge of this office, an attorney, also made the determination whether such collection agencies or attorneys should be authorized to bring suit (Haber 16142-Z-14-16). The accounts, however, would be in the New York office a year before being sent out (Haber 16142-Z-16), and the request for authority to sue by the outside collection agency or attorney would come some three months after the account had been sent from New York (Haber 16142-Z-26). The record does not show how many suits were filed pursuant to these procedures. The witness testifying with respect thereto did not know approximately how many proceedings had been instituted, but testified there were "many" judgments and collections (Haber 16142-Y). This procedure, however, does not cure the deception inherent in the use of attorney letters or other collection forms, directly or impliedly threatening suit, emanating from local offices, which represented a decision to sue had been made by either the local office in question or the lawyer named on the attorney letters (*e.g.*, see CX 150A & B, 151A-Z-15). There was, as far as can be determined from this record, no relationship between the decision in Federated Credit's New York office to refer accounts to outside attorneys or collection agencies or its decision to authorize suit and the prior use by Federated Credit's local offices of forms such as attorney letters or other forms threatening suit.

agreed. We believe the debtor is entitled to this courtesy as his credit may be seriously impaired by permitting his just debts to remain unpaid.

(CX 153-O; see also CX 153P and CX 153Q.)

261. These notices were purchased by respondents from Merchants' Credit Guide and would normally be mailed out by Federated Credit's office (Bodkin 2585). No credit reports were received from Merchants' Credit Guide (Tr. 2586). The implied threat of adverse credit reporting is misleading.

262. Among the collection forms used by Federated Credit was the following notice:

Why risk your job?

The Civil Service Code states that an employee who fails to pay his just obligations may be subject to dismissal.

Pay your full balance now and clear your account with us.

(CX 153F.)[81]

[124] 263. The threat of dismissal in the foregoing notice is misleading; the applicable Civil Service Commission regulation is specific with regard to the kind of financial obligation that may be the basis for any form of disciplinary action. Disciplinary action may range from counseling an employee to the extreme of removal. Further, the regulation expressly states that a "just financial obligation" within its scope is one reduced to judgment by a court or acknowledged by the employee. An employee cannot, under the applicable regulation, be dismissed on the basis of creditor-debtor correspondence (Myers 6028-29) as the form implies.

264. Respondents have also disseminated collection letters threatening criminal prosecution under the Mail Fraud Statutes. In this connection, a form letter under the letterhead Career Institute states as follows:

Dear Mr. Smith:

Your complete lack of interest in your past due account with us leads us to this conclusion: You have used the United States Mail to obtain merchandise without paying for it.

Unless we hear from you by October 18th, your name will be sent to the United States Postal Inspector with our request that he initiate an immediate investigation to determine if you have used the mails to defraud.

Enclosed is an excerpt from the U.S. Criminal Code "Title 18, Chapter 63, Section

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[81] Collection forms in the CX 153 series were used in the period 1965 through 1973 (Bodkin 2581).

1341 & 1342" which describes the penalties that can be imposed on persons convicted of this criminal act. These penalties can include:

1. Fine of $1,000.00
2. Imprisonment of five (5) years

OR BOTH

Your balance is $10.00. Our action will be deferred until October 18, 1969.

J.W. McBurney
Credit Manager

(CX 258B.)

[125] 265. This form impliedly represents that the debtor may be investigated and prosecuted for mail fraud for debts as low as $10.00. The representation does not take into consideration the discretion of the Department of Justice in determining whether to bring suit. It is unlikely that there would be a mail fraud prosecution for amounts as low as $10.00 (Jenkins 6124-25).[82] Moreover, the Department of Justice has never brought a prosecution for mail fraud where a disputed debt was involved (Jenkins 6125). Under the circumstances, the use of the form to make a blanket threat of criminal investigation and prosecution is misleading and deceptive. [126]

VII. RESPONDENTS' SALES THROUGH DISTRIBUTORS

266. Certain of respondents' publications and other products have been sold at wholesale, by subsidiaries of one or another of the respondent corporations, to distributors who resell such publications at retail to members of the public. The record identifies more than 250 such distributors. These distributors may be generally grouped into the following categories:

(a) The "non-Grolier" wholesale customers of Lexicon Publications, Inc. (RX 386 a-f);

(b) The "nonfinanced" wholesale customers of Excelsior Trading Corporation (*i.e.*, those wholesale customers who have not been financed by one of the jobbers of Bunker Hill Service Corporation) (RX 532 a-c);

(c) Those distributors who have purchased products from, and have received financing from, one of the jobbers of Bunker Hill Service Corporation (RX 531 a-b); and

(d) Hemphill Enterprises, Inc. and Jayhill Corporation.

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[82] A Justice Department attorney, who is the head of the Mail and Wire Fraud Unit of the Criminal Division and who had been with the Department of Justice for 23 years, stated that he has no personal knowledge of mail fraud prosecution for amounts as low as $10.00 (Tr. 6124).

A. *The Lexicon Operation*

267. Lexicon Publications, Inc. (Lexicon) is now, and has been since 1965, a wholly-owned subsidiary of respondent Grolier, Inc., with its principal office and place of business in Chicago, Illinois. Since 1965, Lexicon has been engaged in the publication and wholesale distribution of reference publications and related products (Rothschild 14195, *et seq.;* RX 417).

268. The October 1974 list of non-Grolier wholesale customers of Lexicon (RX 386 a-f) includes more than 150 independent distributors from almost every state. Most of these distributors are engaged in the home solicitation sale of reference publications and related products (Tr. 14227). The only business relationship between these distributors and Lexicon is that of purchaser and seller—*i.e.*, Lexicon [127] sells publications at wholesale to such distributors, either on a "cash with order" or "cash within 30 days" basis (Tr. 14227). Lexicon has never financed any of its non-Grolier wholesale customers by acceptance of retail installment contracts or otherwise (Tr. 14230). Lexicon has not monitored, directed or controlled the sales or recruitment practices of any of its non-Grolier wholesale customers (Tr. 14230-31).

B. *The Jayhill-Hemphill Operation*

269. In July 1966, Federated Credit and Hemphill Enterprises, Inc. (Hemphill) entered into an agreement whereunder Federated Credit agreed to finance Hemphill's retail installment contracts involving sales of Grolier products to the general public (CX 118, 119). Hemphill's principal was one Jack L. Hemphill. Certain of the publications sold by, and the sales aids utilized by, Hemphill were purchased from Grolier, Inc. subsidiaries (CX 118A). Grolier, Inc. advanced Hemphill in excess of $1 million in the form of cash and merchandise and, when Hemphill was forced into liquidation, respondents incurred a loss from the transaction (McCabe Deposition, pp. 60, 62).

270. On June 4, 1969, some time after the Hemphill liquidation, the Jayhill Corporation (Jayhill) was appointed as a distributor for Grolier Society's publications (CX 118 A-B). Jack L. Hemphill, also the principal of this corporation, was to devote his full time to selling Grolier Society publications at prices established by Grolier Society and to compensate sales representatives in accordance with the schedules established by this respondent (CX 121A-B).

The distributorship agreement between Grolier Society and Jayhill provided that the latter was to be subject to the former's control "with respect to sales regulations, methods and terms" (CX 121C).

271. While the distributor agreement was in effect, Grolier Society paid a portion of Jayhill's monthly office rental and provided funds in the amount of $500 per month plus commission to Mr. Hemphill (CX 2132A-B). Various respondents' officials visited the offices of Jayhill or Hemphill in the period 1968-1970 (CX 2132B-C). Grolier, Inc. terminated the distributor arrangement with Jayhill on May 11, 1970 (CX 118B). [128]

272. Jayhill's salesmen represented that prospective customers had been selected as a test family for a new program; that their cooperation was being solicited to promote the program (Joy 11357-58); that the prospective customer's opinion on the program was being sought (Margiotta 12451); and that extra or bonus publications would be thrown in if the prospect agreed to finish payments in three years rather than ten years (Joy 11361; Margiotta 12457). Jayhill's sales representatives, in their presentation, also invoked the Grolier name (Margiotta 12451; Joy 11357), and Jayhill's retail contracts contained a picture of the Grolier building (CX 2070A-B).

C. *The Excelsior-Bunker Hill Operation*

273. Excelsior Trading Corporation (Excelsior) is now, and has been since 1972, a New York Corporation engaged in the wholesale distribution of reference publications. Since its formation in 1972, Excelsior has been a wholly-owned subsidiary of respondent Richards (Ryan 5823, 5826).

274. Bunker Hill Service Corporation (Bunker Hill) is now, and has been since 1972, a New York corporation engaged in the business of financing certain jobbers or wholesalers of encyclopedias and other reference publications. Since its formation in 1972, Bunker Hill has been a wholly-owned subsidiary of respondent Richards (Ryan 5826).

275. Excelsior and Bunker Hill were created in 1972, as the basis for a distributor system which would convert the Richards business into a wholesale operation after it was determined that this subsidiary would no longer sell directly to the consumer.[83] The purpose of instituting this system was to permit certain Richards' employees to remain in the reference book business (Ryan 5826)[84] and [129] to preserve respondents' investment in the American

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[83] Continental Publications Incorporated had been accepted as a distributor in 1970, as a pilot program to test the feasibility of such a distribution method (Hauswirth 11016).

[84] Financed distributors in this category will sometimes be referred to hereinafter as the "Richards' spinoff distributors."

Peoples Encyclopedia (Murphy 16467–68). The plan for the distributor network was presented to the Chairman of the Board of Grolier, Inc. and approved (Ryan 5826).

276. The primary problem in organizing the distributor program was to arrange financing.[85] Two companies were created by respondents: the first, a company to wholesale the books (Excelsior); the second, a company to finance the paper (Bunker Hill) (Ryan 5826). Under the distributor system, in any one transaction, four companies performed the functions Richards had previously performed, *viz.,* two Richards subsidiaries to wholesale the books and finance the transactions and, further down the chain, the jobber and the distributor (Pardee 11077).

277. Jobbers were envisaged as the key to the distribution system (Ryan 5837–38). They were selected for their experience in collections and to make sure that the sales being financed were quality sales which would be profitable (Kohen 14336–37).

278. Under this system, the distributor, who sells door-to-door to the consumer, buys his merchandise from the jobber and assigns the consumer retail installment contract or paper to the jobber. The distributor, when he assigns the paper, sends the sales contract to the jobber along with the check for the merchandise (Ryan 5838–39).

The jobbers, in turn, assign the orders to Bunker Hill which reviews the orders. Bunker Hill, if the order is accepted, sends the jobber a check for 60 percent thereof. The jobber transmits an advance to the distributor. The jobber sends a check to Excelsior for the merchandise (Ryan 5839). Excelsior drop-ships the merchandise to the subscriber (Kohen 14361). In short, Bunker Hill finances the jobbers, who, in turn, finance the distributors (Ryan 5837). [130]

279. The jobber does all the collecting for the distributor and the distributor is only charged on those accounts on which payment has not been made (Ryan 5833, 5839–40). Jobbers retain a certain percentage of each contract sold to the consumer as a reserve for bad debts. If an account becomes delinquent and is not collected by the jobber, the jobber returns the account to the distributor and charges the reserve (Pardee 11153t–u).[86]

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[85] There are many small book distributors in the United States. Some are successful; the failures to a considerable degree are attributable to financing which is very difficult to get (Ryan 5825–26).

[86] The mechanics of the collection process in the case of one jobber, American Acceptance Corporation, may be outlined as follows:

The contracts are payable in 35 months and American Acceptance collects thereon (Kohen 14319). It submits all collections to Bunker Hill as repayments on the loan (Kohen 14320). If an account becomes uncollectable, the distributor repurchases the contract from American Acceptance which repurchases the contract from Bunker Hill (Kohen 14320–21).

American Acceptance submits the total amount collected to Bunker Hill. At the end of the month, Bunker Hill charges an interest and service charge varying from $2.55 to $2.75 for every open account. Bunker Hill applies 60 percent of the collections to the advance previously given to American Acceptance. American Acceptance receives

(Continued)

280. Jobbers sell at cost to the distributors they finance and make no profits on such sales (Kohen 14358). The only profit made by jobbers with respect to financed sales is the amount withheld by the jobber from collections returned by Bunker Hill (Kohen 14359).

281. In the period from 1972 to 1976, Bunker Hill financed four different jobbers: Paragon Service Company of Atlanta, Georgia; American Acceptance Company of Milwaukee, Wisconsin; Columbia Financial Corporation of Springfield, Virginia; and Allied Acceptance Corporation of Los Angeles, California (RX 531 a-b). [131]

282. Officials of Richards, including its President, John Ryan, recruited and encouraged Richards' employees and former employees to become distributors and jobbers (Kohen 14335-36; Ryan 15998; Berry 15729, 15737; Pardee 11077-78, 11083).

In fact, most of Richards' key sales personnel became distributors (Ryan 15998).[87] And the individuals who became jobbers were basically Richards' personnel experienced in both sales and administrative work (Ryan 5837-38). Certain of the jobbers had previously supervised at Richards the personnel who later became distributors (Kohen 14346-47; Berry 15721).

283. Richards' personnel gave advice and help to former Richards' employees in setting up and operating their distributorships (Ryan 15998; Pardee 11117-19). In this connection, prospective distributors were provided with a document outlining the steps to be taken in forming such distributorships (Pardee 11085-87). In the case of one distributor, his retail contract was drawn up by a member of the Grolier, Inc. legal staff (Pardee 11093, 11119, 11154-a).

284. Distributors were offered a commission to collect old Richards accounts still outstanding and allowed to remain in the Richards office rent-free until the leases expired (Ryan 16002-03, 16057). Arrangements were also made to permit the distributors to acquire the furniture and fixtures in the Richards office under a rent purchase agreement (Ryan 16003). And sample forms were provided to the distributors for their use (Pardee 11119). The President of Bunker Hill helped one distributor to set up his accounting records (Pardee 11119).

285. A standard contract is in use between Bunker Hill and the jobbers (Ryan 5847). This contract was of the same format as that used between the jobbers and the distributors (Ryan 5848). The

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40 percent less the $2.55 to $2.75 service charge per account. This gives the jobber approximately 23 percent of the amount collected of which the distributor receives 10 percent. The jobber retains approximately 13 percent (Kohen 14355-57).

[87] In one case, there was apparently a wholesale transfer of personnel from Richards to the new distributor (Sander 14452-53).

services of the Grolier Legal Department were utilized in developing this contract (Ryan 5848). [132]

286. Respondents and their officials have no equity interest in the distributor (Ryan 5838).

Every distributor was to set up his company with his own money. No money came from the President of Richards, Richards, or Grolier, Inc. (Ryan 5838; Caldwell 13399-400; Berry 15712).

Such distributors have paid the ordinary everyday expenses of their business, with the exception in some instances of short term rent-free occupancy of Richards' premises (Sander 14444; Berry 15723; Pardee 11153-w; Hauswirth 11033, 11048).

287. The sales and recruitment practices used by distributors were formulated by their own officials without outside direction (Pardee 11153-o-p-q; Hauswirth 11035-37, 11043; David 13534-35; Berry 15715-16; Sander 14447-50; Liquie 10972-73; Caldwell 13398). The recruiting practices followed by certain distributors were similar to those formerly utilized by Richards (Berry 15745; Caldwell 13419). The sales presentations were similar or essentially the same as those formerly utilized by Richards (Pardee 11154-f; David 13562-63; Sander 14491-93; Berry 15773; Caldwell 13421-30). The continuation of such practices by the distributors, however, may be ascribed to their prevalence in the industry (Caldwell 13427).

288. These distributors have not held themselves out as representing the respondents in their sales presentations (Pardee 11154-b; Liquie 10984; Sander 14455-57; David 13547-49; Berry 15715; Caldwell 13398). Such distributors were actual or potential competitors of Grolier Interstate (Pardee 11098). [133]

DISCUSSION

Jurisdictional And Procedural Issues

Respondents challenge the Commission's jurisdiction with respect to sales recruitment practices on the ground that they are local, not trade practices, and, therefore, not within the Commission's jurisdiction. The recruiting activities, however, are an integral part of respondents' interstate operations. The contention that such activities are local and not trade practices is without merit and is rejected. See *Encyclopedia Britannica, Inc.*, Dkt. 8908 (Commission Opinion and Order, March 9, 1976 [87 F.T.C. 421]).

Respondents also urge on the basis of procedural grounds that no initial decision should be rendered at this time. They contend that (1) the Commission erred in denying respondents' 1973 petition for the institution of Trade Regulation Rule proceedings; (2) the administrative law judge erred in denying respondents' 1975 motion for stay of the present proceeding pending a reopening of the proceedings in *Americana Corporation*, Dkt. 5085; (3) the administrative law judge and the Commission erred in denying respondents' 1976 motion for disqualification and removal of the administrative law judge; (4) the administrative law judge erred in denying respondents' 1975 requests for discovery from the Commission; and (5) the administrative law judge and the Commission erred in denying respondents' 1972 motion to dismiss for failure to join indispensable parties.

The various rulings complained of and the reasons therefore are on the public record. Further discussion at this time is unnecessary. The initial decision will issue. The Commission will be in a position, where appropriate, to consider or reconsider these questions on appeal.

Substantive Issues

The allegations of the complaint have already been summarized (pp. 1–3, *supra*). Suffice it to say that the practices alleged unlawful have been considered countless times by the Commission in the past. The law in this area is well settled; it requires no extended discussion. A summary of the applicable general principles follows. [134]

Capacity to deceive and not actual deception is the criterion by which practices are tested under the Federal Trade Commission Act. *Goodman* v. *FTC*, 244 F.2d 584, 604 (9th Cir. 1957); *Regina Corp.* v. *FTC*, 322 F.2d 765, 768 (3rd Cir. 1963); *FTC* v. *Sterling Drug, Inc.*, 317 F.2d 669, 674 (2nd Cir. 1963)[88] *Charles of the Ritz Dist. Corp.* v. *FTC*, 143 F.2d 676, 680 (2nd Cir. 1944); *Progress Tailoring Co.* v. *FTC*, 153 F.2d 103 (7th Cir. 1946). The fact that some customers are not misled is irrelevant if the practices under consideration have the tendency to mislead. *Mohawk Refining Corp.* v. *FTC*, 263 F.2d 818, 821 (3d Cir. 1959), *cert. denied*, 361 U.S. 814 (1959); see also *Thiret* v. *FTC*, 512 F.2d 176, 180 (10th Cir. 1975).

In determining the meaning of an advertisement, a piece of promotional material, or a sales presentation, the important criterion is the net impression that it is likely to make on the general populace. *National Bakers Services, Inc.* v. *FTC*, 329 F.2d 365, 367 (7th Cir. 1964). In ascertaining the impression created, the Commission need not look to the technical interpretation of each phrase but, rather, looks to the overall impression likely to be made on the buying public. *Murray Space Shoe Corporation* v. *FTC*, 304 F.2d 270, 272 (2nd Cir. 1962). A statement may be deceptive even if the constituent words may be literally or technically construed so as not to constitute a misrepresentation. *Kalwajtys* v. *FTC*, 237 F.2d 654, 656 (7th Cir. 1956), *cert. denied*, 352 U.S. 1025 (1957); *Sterling Drug, Inc.* v. *FTC*, *supra*. Advertisements which are capable of two meanings, one of which is false, are misleading. *Rhodes Pharmacal Co., Inc.* v. *FTC*, 208 F.2d 382, 387 (7th Cir. 1953), *modified on other grounds*, 348 U.S. 940 (1955). Such statements will be construed against the advertiser. *Murray Space Shoe Corporation* v. *FTC*, 304 F.2d, *supra* at 272. [135]

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[88] ". . . In order best to implement the prophylactic purpose of the statute, it has been consistently held that advertising falls within its proscription not only when there is proof of actual deception but also when the representations made have a capacity or tendency to deceive, i.e., when there is a likelihood or fair probability that the reader will be misled. . . ." *FTC* v. *Sterling Drug, Inc.*, 317 F.2d, supra at 674.

The Commission is not confined to proscribing affirmative misrepresentations. The literal truth employed in a particular context may be used to deceive and deception, moreover, may be accomplished by innuendo as well as by outright false statements. *Bockenstette* v. *FTC*, 134 F.2d 369 (10th Cir. 1943); *Bakers Franchise Corporation* v. *FTC*, 302 F.2d 258, 261 (3d Cir. 1962); *Regina Corp.* v. *FTC*, 322 F.2d, *supra* at 768.

Furthermore, "[r]epresentations can be contrived to mislead not only by what they contain but by what they omit." *Manco Watch Strap Co. Inc.*, 60 F.T.C. 495, 510 (1962). The Commission may utilize its expertise in determining what facts are material to consumers and thus determine the situations in which material facts have not been disclosed. *Pfizer Inc.*, 81 F.T.C. 23, 58 (1972). The Commission has ruled:

> In order to prevent this type of deception, the Commission is often obliged in its orders to go beyond conventional negative prohibitions and to require disclosure of material facts previously not disclosed to prospective purchasers. If affirmative disclosure is the effective antidote to deception, it is a remedy the Commission may - even must - prescribe. *Manco Watch Strap Co.*, 60 F.T.C., *supra* at 510.

An order requiring affirmative disclosure, moreover, "is not an extraordinary or unusual remedy to be applied only in extreme cases." *S.S.S. Co.*, 73 F.T.C. 1058, 1088 (1968).

The Commission in evaluating the tendency of language to deceive "should look not to the most sophisticated readers but rather to the least." *Exposition Press Inc.* v. *FTC*, 295 F.2d 869, 872 (2nd Cir. 1961), *cert. denied*, 370 U.S. 917 (1962). Also applicable here is the principle that "[t]he likely impact on those who view the advertising even casually or distracted by other activities must be taken into account." *Giant Food, Inc.*, 61 F.T.C. 326, 346 (1962), *affirmed*, 322 F.2d 977 (D.C. Cir. 1963), *cert. denied*, 376 U.S. 967 (1964).

Finally, "[t]he law is violated if the first contact or interview is secured by deception . . . even though the true facts are made known to the buyer before he enters into the contract of purchase." *Carter Products Inc.* v. *FTC,* 186 F.2d 821, 824 (7th Cir. 1951); *Exposition Press Inc.* v. *FTC,* 295 F.2d, *supra* at 873. [136]

The significant issues in this proceeding relate to remedy. The issues requiring consideration are: (1) whether the violations proven are substantial; (2) whether no remedy should be imposed because of abandonment; and (3) if an order issues, what is the appropriate remedy.

Remedy

1. *Parent Company Responsibility*

The first question in considering the reach of the order is whether the parent company, Grolier, Inc., can be held responsible for the violations of law found herein. A parent company's liability for the actions of its subsidiaries is not governed by the common law rule restated in *National Lead Co.* v. *FTC,* 227 F.2d 825, 829 (7th Cir. 1955), *rev'd. on other grounds,* 352 U.S. 419 (1957).[89] The Commission need not find such complete control by the parent that the subsidiary is a mere tool and its corporate identity a mere fiction. The Commission has expressly rejected the contention that so stringent a standard applies holding:

> Manifestly, where the public interest is involved, as it is in the enforcement of Section 5 of the Federal Trade Commission Act, a strict adherence to common law principles is not required in the determination of whether a parent should be held for the acts of its subsidiary, where strict adherence would enable the corporate device to be used to circumvent the policy of the statute."

(*Beneficial Corp., et al.,* CCH 1973-76 Transfer Binder, ¶20,959 (1975), *modified on other grounds,* Slip Op. (3rd Cir. 1976).)

In determining parent company liability, the Commission examines "the pattern and framework of the whole enterprise." *Art National Manufacturers Distributing Co.* v. *FTC,* 298 F.2d 476, 477 (2nd Cir. 1962), *cert. denied,* 370 U.S. 939 (1962); *Beneficial Corp., supra.* The applicable standard has been met if the facts demonstrate even latent control. *Beneficial Corp., supra.* As the Sixth Circuit has stated: [137] [W]here a parent possesses latent power, through interlocking directorates, for example, to direct the policy of its subsidiary, where it knows of and tacitly approves the use by its subsidiary of deceptive practices in commerce, and where it fails to exercise its influence to curb illegal trade practices, active participation by it in the affairs of the subsidiary need not be proved to hold the parent vicariously responsible. Under these circumstances, complicity will be presumed.

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[89] Cited in Respondents' Reply Brief, p. 2.

P. F. Collier & Son Corp. v. *Federal Trade Commission,* 427 F.2d 261, 270 (6th Cir.), *cert. denied,* 400 U.S. 926 (1970).

Those criteria have been met here. Grolier, Inc., through interlocking directorates and management, controls its subsidiaries. It has actively intervened in their sales and employment activities.[90] In this connection, it is significant that the parent company could terminate a subsidiary's local sales office when it became an embarrassment, and that a parent official could cancel the sales contracts of subsidiaries without their acquiescence. In addition, the record shows that, through its surveillance activities, the parent company had actual knowledge of the law violations of its subsidiaries. The Grolier Interstate reorganization in 1971, terminating the operating life of the then direct-selling subsidiaries, is wholly inconsistent with respondents' assertion of corporate separation between parent and subsidiary. The parent-subsidiary operation constituted an interrelated enterprise. The financial support and services furnished by Grolier, Inc. were essential to the operation of the subsidiaries. Being responsible for their actions, Grolier, Inc. had the [138] responsibility of effectively preventing violations of law by the personnel of its subsidiaries.

Where the parent company is shown liable for the acts of its subsidiaries because of the power to control, it is unnecessary to demonstrate that the practices alleged illegal were expressly authorized by the parent or that it actively participated therein. See *P. F. Collier & Son Corp.* v. *FTC,* 427 F.2d, *supra* at 270. It is no defense that the misrepresentations of respondents' sales representatives may have been unauthorized or contrary to the announced policy of respondents. Respondents are bound by the acts of the salespersons and other employees they choose to retain if such acts are within the actual or apparent scope of their authority. When respondents put sales representatives on the street, they are clothed with apparent and, in fact, real authority to speak for their principals. This is equally true of local management officials in charge of recruiting and training respondents' sales representatives. See *Goodman* v. *FTC*, 244 F.2d, *supra* at 592. The offending conduct of the sales representatives or local management may have been unauthorized and even condemned and discouraged by respondents. Such conduct, within the actual or apparent scope of their authority, nevertheless subjects the employers to the jurisdiction of the Commission and its cease and desist order. *Id.* at 592; see also *Parke, Austin & Lipscomb, Inc.* v. *FTC*, 142 F.2d 437, 440 (2nd Cir. 1944). Unsuccessful attempts to prevent misrepresentation by his authorized agents will not put the principal beyond the reach of the Federal Trade Commission Act. *Goodman* v. *FTC*, *supra* at 592.[91] [139]

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[90] Consider, for example, the directive of Grolier, Inc.'s President to all subsidiaries, dated October 21, 1969:

> "It has been decided that all subsidiaries will cease using the Vacation Certificate by December 31, 1969. The time limit of December 31st was set to give you time to phase them out" (CX 127).

The directive clearly demonstrates the parent company's assertion of the right to control the details of its subsidiaries' sales operation.

Respondents contend that no order may issue against any of them unless supported by separate findings as to the sales and recruiting practices of each respondent subsidiary.[92] The contention is rejected. As already noted, the respondent subsidiaries are subject to the control of the parent company, which has actively intervened in their operations. The subsidiaries' operational lives may be cut short at any time by the parent and another subsidiary substituted in their place. The record, moreover, shows that the sales operations of the subscription book companies and the mail order subsidiaries in their respective spheres have followed the same basic themes.[93] As a

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[91] "Thus the courts take the view that the principal is bound by the acts of the salesperson he chooses to employ, if within the actual or apparent scope of his authority, even *when unauthorized*. As said by the Court of Appeals for the Second Circuit:

> " 'But however unauthorized the offending conduct of the salesmen may have been and however condemned and discouraged by their superiors, it still was conduct which subjects the employers to the jurisdiction of the Commission and to its cease and desist order.'

"In a later case the same court, in dealing with misrepresentations in conjunction with the sale of books, held the principal responsible because the salesmen *were his authorized agents*. This, despite the fact that the Commission found that the misrepresentations were made in *violation of direct instructions*. The Court summed up the matter in these words:

> " 'They were nevertheless the authorized agents of the corporate petitioners * * * to sell the books. The misrepresentations they made *were at least within the apparent scope of their authority and part of the inducement by which were made sales that inured to the benefit of the corporate petitioner*. Unsuccessful efforts by the principal to prevent such misrepresentations by agents will not put the principal beyond the reach of the Federal Trade Commission Act.' (Emphasis added.)" (*Id.* at 592–93).

[92] Respondents' proposed findings, however, generally are not framed so as to assist in the kind of analysis which, in their reply memorandum, they consider essential.

[93] This is demonstrated by the following tables referring to certain sales presentations in the record and to respondents' 1969 telephone survey:

Sales Presentations

	Spencer	*Americana*	*Grolier Society*	*Richards*	*Hinkley*
Misrepresent Purpose of Contact or Visit	871F, G	446A 447A–B 448A	563J, P	971B 956A	1023A
Help and Cooperation Pitch	439C–D 439Z–9	446C 447B	563J, M, R	971C 956A, B	1023A, B

(Continued)

result, findings going to the collective [140] operations of the subsidiaries are sufficient to bind the parent company. Indeed, if the Order is to have any meaning, it is the parent company and its successors which must be bound. Similarly, the subsidiaries, in view of their subservience to Grolier, Inc. and the fact that the parent-subsidiary operation must be viewed as a whole,[94] are also bound by findings going to the entire operation. [141]

2. *The Practices Were Substantial*

On the basis of the number of consumer and ex-salesperson witnesses appearing in this proceeding, respondents urge that the evidence of violation is *de minimis* and that the case should be dismissed for that reason. The argument is without merit. The number of such witnesses testifying is not the sole measure of the extent of the violations. In fact, the Commission is not required to produce any customers to testify as to their deception.[95] Respondents' 1969 telephone surveys show that the misrepresentations in connection with their in-home presentations were substantial, and that they were aware of that fact (Finding 52). The record shows that respondents' sales representatives were trained by local office management to use the prohibited practices such as disguising the

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Savings Claims	871N 439Z–8–9	447I		964K-L	1023B
10-Year Conversion Representations	871P		563N, R	964P–Q	

1969 Telephone Survey

	Americana	*Spencer*	*Grolier Society*	*Hinkley*
Excessive Savings	82K, 83E, 95E	77D, 79D, 83I, 94H, 106E, 116K,	77C, 79C, 81G, 83F, 90D, 103D 115E	81J, 81N, 91H, 101F, 113G
Selectivity	85E, 117E, 117F	82G, 86H, 105H, 110C, 111M, 114I 115"O"	77C, 82E 92"O", 101D, 109D, 11F, 116G	105F, 108F, 111I
Free (Bonus) Merchandise	81E, 100E, 116E	87J, 87Q, 102F, 103H, 112J, 116K	84G, 86D, 94D, 95G 97D, 104E, 112E	85I, 89H 91H, 92K 104G, 112H 113D

Respondent Grolier Interstate, in 1971, became the successor of the former direct-selling subsidiaries.

[94] It is significant that Grolier, Inc. represented to consumers in its institutional advertising that the parent company assumed responsibility for the sales practices occurring in the field (Finding 44).

[95] "That the Commission did not produce consumers to testify to their deception does not make the order improper, since actual deception of the public need not be shown in Federal Trade Commission Proceedings." *Charles of The Ritz Dist. Corp.* v. *FTC*, 143 F.2d, *supra* at 680.

sales purpose of the contact with consumers by representing that they were interviewers, field counselors, advertising men, etc. The written sales presentations in this record, which respondents' sales representatives were trained to use, demonstrate that the practices under consideration were not the isolated practices of a few. (See generally Section IV-G, *supra.*)[96] The record further shows that as late as 1973 to 1974, respondents' regional vice presidents were being terminated for permitting continuation of, or for failure to, eradicate the violations under consideration here. The need to terminate management officials on this level further documents the fact that the violations occurring were not insubstantial. [142]

In the case of the continuity programs, the basic violation was the failure to advise the consumer that he would receive at one stage of the program a bulk shipment of books rather than the single volume expected. Respondents commenced giving an explicit disclosure of that fact in March 1971. The mailings in the preceding years did not carry such a disclosure. In 1970 alone, respondents had 398,253 new orders for their continuity programs (Finding 218). The number of attendant initial mailings without the disclosure must have been substantial.

The law violations in the debt collection area also were not insubstantial or *de minimis.* The record shows, for example, that the use of attorney letters, directly or impliedly threatening legal action by lawyers who had not originated the letters or reviewed the accounts, or who were not authorized to file suit, was pervasive.

Finally, the testimony of the Government witnesses appearing herein, both ex-salespersons and consumers, on their experiences with respect to recruitment practices, training and the type of sales presentation given is uncontradicted. In the case of the ex-sales representatives, no testimony from their superiors was presented to show that they had erred in their testimony as to the sales training received. Their testimony, moreover, is corroborated by the contemporaneous documents (*e.g.,* CX 563; see n. 93, *supra*).

The record establishes a pattern of unfair and deceptive acts and practices on the part of these respondents.

3. *Discontinuance*

Respondents also contend that no order should issue since the challenged practices have been discontinued. Respondents did send policy directives to their employees to stop various of the misrepresentations involved herein, including misrepresentation of the purpose of the salesman's call.[97] The [143] policy of prohibiting such practices was not, however, effectively executed. Substantial violations occurred at the time such directives were sent out and continued thereafter. The reason that such efforts at reform were not effective is that respondents' field management has historically not been responsive to direction from the head office (Findings 50, 51, *supra*).

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[96] Consider, for example, CX 563A-V, a sales manual prepared by a Grolier Society Vice President which was in use for several years in the Los Angeles area and which salesmen were instructed to follow (Long 2835-39). The manual trained sales representatives in how to disguise the sales purpose of their contacts with the consumer. *E.g.*, CX 563I. (See also Findings 118-20, 128-30.)

Respondents' Assurance of Voluntary Compliance covering many of the recruitment and sales practices involved herein was accepted in July 1967.[98] Substantial violations by respondents nevertheless continued in the succeeding period (*e.g.*, Findings 50, 51, 101, 113, 135, 191–94).[99] By the end of 1970, some three years later, the situation was such that in order to control such violations, respondents deemed it necessary to have a complete corporate overhaul, reorganizing the activities of the direct-selling subsidiaries into one (Finding 41). This reorganization commenced in January 1971, but the buildup of the headquarters staff necessary to achieve the required control of the sales organization did not commence until 1973 (Findings 41, 51). And, as already noted, at least some of respondents' management continued to be unresponsive to policy directives in this area as late as 1973 to 1974. The formal complaint in this proceeding issued in 1972. Under the circumstances, the record does not support dismissal of the charges on the ground of abandonment. See generally, *U.S.* v. *Oregon State Medical Society*, 343 U.S. 326, 333 (1952); *Coro, Inc.* v. *FTC*, 338 F.2d 149, 153 (1st Cir. 1964), *cert. denied*, 380 U.S. 954 (1965). A cease and desist order is required to assure effective control by respondents over their field management and sales representatives to prevent repetition of the law violations within the scope of this proceeding. [144]

Respondents assert the evidence does not reflect current practices. The age of the evidence, however, does not preclude the issuance of an order. As the Sixth Circuit held in *P. F. Collier & Son Corp.* v. *FTC*, 427 F.2d, *supra* at 275:

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[97] *E.g.*, RX 63, Memo dated March 15, 1968; RX 65, Memo dated May 14, 1969; RX 66, Memo dated May 15, 1969; RX 68, Memo dated May 29, 1969; RX 69, Memos dated July 17 and 23, 1969. These memoranda, cited in respondents' posthearing memorandum, pp. 38–39, pertain to Richards. A major reason for not including Richards in the 1971 Grolier Interstate reorganization, however, was the fact that it had generated too many sales problems (see Finding 42 and n. 13).

[98] Respondents have with some frequency been involved in Commission proceedings. A cease and desist order was entered against the Americana Corporation in 1949, and a number of civil penalty suits have been filed thereunder. In 1964, a consent order relating to debt collection practices was accepted in the case of Grolier Enterprises, Dkt. C–753 [65 F.T.C. 901]. In 1966, the Commission issued a proposed complaint relating to many of the practices involved herein. That proceeding was resolved by acceptance of the Assurance of Voluntary Compliance in 1967.

[99] The evidence of violation in this proceeding relates primarily to the period 1968–1970.

> . . . The fact that this evidence may be old, per se, does not mean that an order issued upon it is vitiated. Where an illegal trade practice is once proved against an enterprise, and is capable of being perpetuated or resumed, it may be presumed to have been continued, and an order may issue to prevent it, even upon a showing that it has been discontinued or abandoned. See *e.g.*, Perma-Maid v. Federal Trade Commission, 121 F.2d 282 (6th Cir. 1941).

The Order

Respondents contend that the imposition of any cease and desist orders in the encyclopedia industry is inherently inequitable and unworkable. They assert that insofar as an order seeks to regulate or restrain the activities of sales representatives by provisions directed against their employers, this simply results in the sales representatives transferring to unregulated companies. Respondents argue that, should an order issue, there would be a resultant serious erosion of their sales force leaving them at a competitive disadvantage with respect to companies not so regulated. They further contend that sales representatives transferring to other firms would simply continue the prohibited practices. Accepting the argument that no order should issue for that reason would preclude Commission action to prevent deception in door-to-door selling in any industry. The contention must be rejected. The fact that an order may restrict more severely a firm subject to its provision than its competitors does not justify the failure to take remedial action where warranted. At best, such a situation affords the basis for an argument that respondents' competitors should be dealt with likewise, not that respondents should escape. See *P. F. Collier & Son Corp.* v. *FTC*, 427 F.2d, *supra* at 276. [145]

The determination to proceed against particular members of an industry in an adjudicative proceeding is well within the Commission's administrative discretion. *Moog Industries, Inc.* v. *FTC*, 355 U.S. 411 (1958). In any event, the Federal Trade Commission Improvement Act has considerably broadened the reach of final cease and desist orders. As a practical matter, Section 205 of the Statute[100] gives such orders the effect of rules binding nonparties provided they have actual notice. To a considerable degree, this diminishes the competitive disadvantage which may result from the imposition of a cease and desist order. Furthermore, pursuant to the provisions of Paragraph V of the Order to be issued herein, respondents' sales representatives will be furnished with a copy of the Order. Having received actual notice, such sales representatives will be liable, pursuant to Section 205, for violation of its provisions.

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[100] "(B) If the Commission determines in a proceeding under subsection (b) that any act or practice is unfair or deceptive, and issues a final cease and desist order with respect to such act or practice, then the Commission may commence a civil action to obtain a civil penalty in a district court of the United States against any person, partnership, or corporation which engages in such act or practice—

"(1) after such cease and desist order becomes final (whether or not such person, partnership, or corporation was subject to such cease and desist order), and

"(2) with actual knowledge that such act or practice is unfair or deceptive and is unlawful under

(Continued)

Turning to the specific provisions of the Order, it should be noted that the cease and desist order recently issued by the Commission in *Britannica, supra,* with some exceptions, covers the violations proven in this proceeding. Competitors similarly situated should be treated alike provided that the remedy imposed in each instance is effective. Sound administration dictates in this instance that the remedy imposed be consistent with the most recent Commission precedent in this area. Therefore, absent a compelling reason to the contrary where the violation is the same and the facts similar, the *Britannica* order should be followed herein. Furthermore, the provisions of the Federal Trade Commission Improvement Act, giving the force of rules to final cease and desist orders, if there is actual notice, also argue for uniformity of treatment. [146]

Respondents strenuously object that the affirmative relief provisions sought by the Commission's staff will be injurious to their legitimate business operations and ineffective in terms of preventing illegal practices. The Comission has authority to require affirmative undertakings or actions in its orders. "Remedies of this nature are often necessary to prevent recurrence of an illegal practice or to cure the ill effects of such a practice." *Curtis Publishing Co.,* 78 F.T.C. 1472, 1513 (1971). Whether such a remedy is appropriate in a particular proceeding depends on the facts and circumstances of each case.

1. *Order Provisions Relating To Recruiting Practices*

Respondents' recruiting practices have been challenged on the ground that they failed to disclose or misrepresented the nature of the position offered; that they misrepresented that prospective recruits were being hired as management trainees; and that they deceptively described the compensation offered. The proposed order would impose affirmative disclosure requirements on respondents' recruiting, both in the recruiting advertisements and at the time of the first personal interview. Respondents deny that their recruiting

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subsection (a)(1) of this section.

In such action, such person, partnership, or corporation shall be liable for a civil penalty of not more than $10,000 for each violation."

advertisements are deceptive. They object particularly to the imposition of affirmative disclosure requirements in the case of the recruiting advertisements stating that all relevant facts are disclosed at the time of initial interview.

Respondents utilize blind advertisements in their recruiting program which do not describe the nature of the position offered *i.e.*, door-to-door or in-home selling, the name of the employing company, or the product involved.

Certain advertisements have misstated the nature of the job offer with terms such as linear programming, instructor, public relations work, etc. (Findings 59, 60). The record demonstrates that a substantial portion of the public does not desire employment as an encyclopedia salesman selling in-home or door-to-door (Findings 62, 64). For that reason, respondents do not disclose in their blind advertisements that door-to-door selling is involved in the position offered. An advertisement making such disclosure, according to the testimony of respondents' officials, would not draw the type of applicant wanted (Finding 62). In short, respondents' advertisements were designed to draw responses from persons [147] who would not have answered such advertisements had they disclosed the type of position offered (Finding 64). For that reason, alone, the blind recruitment advertisements are deceptive. *Britannica, supra.* [101]

Subsequent disclosure of the relevant facts at the time of the first personal interview does not serve to cure the initial misrepresentation. See *Carter Products, Inc.* v. *FTC*, 186 F.2d, *supra.* Not all of respondents' recruits, moreover, were fully apprised of the nature of the position at the time of the initial interview (Findings 74–76). For example, certain of the less sophisticated trainees, on the basis of the sales presentation they were taught, believed that they were engaged in such fields as advertising or interviewing (Finding 75).

The foregoing demonstrates the need for requiring affirmative disclosure of the nature of the employment offered in the recruitment advertisements and at the initial interview.

Respondents did not have a formal management training program as such available to those who responded to advertisements offering such training. The offer of management training implies a specific program for that purpose and that those who are accepted will be placed in such program when hired. As far as can be determined from this record, many recruits responding to such offers were treated no differently than other trainees. Under the circumstances, such representations were deceptive.[102] (Findings 65-67.) [148]

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[101] As stated in the *Britannica* initial decision adopted by the Commission:

"It is clear that the deception fostered by respondent's 'blind' advertisements is successful in bringing persons to respondent's offices who would not have come if they had known that the position offered involved door-to-door selling, which is the admitted reason respondent uses blind advertisements. Therefore, such advertisements have the tendency and capacity to deceive a substantial number of potential job applicants, and to cause applicants to invest time, energy and money in investigating job opportunities in which they would not otherwise have been interested" (P. 83).

Respondents' recruitment advertisements have utilized offers of guaranteed monthly incomes (Finding 68). The advertisements containing such representations, however, do not spell out the conditions which must be met before such compensation will be paid (Finding 70). Sometimes, such conditions were not fully disclosed at the initial interview (Finding 77). In addition, respondents' trainees were frequently discouraged by local management from insisting on the guaranteed income advertised and were pressured to accept commissions instead (Finding 80).[103] Some guaranteed salary payments were made (Finding 84). However, the guaranteed or stated salary was not available for an open-ended period as the advertisements implied. It was respondents' policy to make such guaranteed payments available only for a limited period, generally not exceeding a month (Finding 85). The unqualified representation that a guaranteed income was being offered was misleading.

The use of the management training and guaranteed income representations were interrelated with respondents' use of blind advertisements. These representations reinforced the deception inherent in the failure to disclose the nature of the position offered. As a result, an Order should issue in this case, as in *Britannica*, prohibiting further misrepresentations in these areas and requiring disclosure of the conditions and qualifications applicable to any offers of management training or compensation.

The recruiting practices found illegal in this proceeding are essentially identical to those prohibited by the Commission in *Britannica*. The provisions in that order pertinent to recruiting practices will be applied herein. Complaint counsel propose, in a departure from the *Britannica* order, that respondents be prohibited from making any representations in their recruiting advertisements that the compensation consists [149] of a stated salary or guaranteed income unless 30 percent of the persons holding similar positions in the office making the offer of employment have received an equivalent or greater income during the preceding 12 months. A similar provision was rejected by the Commission in *Britannica* (at p. 7). In rejecting that provision, the Commission stated:

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[102] Paragraph I A(2) of the Order prohibits representations that persons will be trained as management trainees "unless, in fact, a formal management training program is available to persons accepting employment on the basis of such representations." The prohibition of such representations is qualified in the Order since respondents are apparently now instituting a formalized corporate sales management training program (Toman 16306).

[103] Many trainees responding to advertisements promising guaranteed incomes were unable to earn commissions equal to the advertised guarantees. This is not surprising. The blind advertisements under consideration here may be expected to recruit a large number of people with little or no aptitude for direct selling or ability to get in the door to make a presentation.

> . . . We have deleted this provision. The modified order bans misrepresentations of guaranteed income. A related order provision requires affirmative disclosure, prior to the time respondent enters into a guaranteed income employment contract, of the percentage of persons employed in similar positions who earn the stated income. The ban on misrepresentations, coupled with the disclosure, should suffice to correct respondents' guaranteed income deceptions.

That reasoning is applicable here.[104] Complaint counsel's contention is, therefore, rejected.

2. *Order Provisions Requiring Disclosure of Objective of Respondents' Contact with Consumers When the Purpose Is To Sell*

Lead Gathering

Securing leads to prospective customers by offers of free information, gifts, or the opportunity to enter a contest, without disclosing that the recipient may be subjected to a sales presentation as a result of responding to such offers, is unfair and deceptive. It is now established that "Recipients of 'free' information solicitations are entitled to know what strings are attached; that a salesman may call; that they will be subjected to a sales pitch." *Mather Hearing Aid Distributors, Inc.*, 78 F.T.C. 709, 735 (1971); *Britannica, supra* at 10. Paragraphs II A and B of the Order will require the necessary disclosures. [150]

The Card-at-the-Door Requirement

The requirement that encyclopedia salesmen affirmatively disclose, at the time of initial contact with the consumer at his home, that they are sales representatives and that the purpose of the call is to make a sale is not a novel one. In fact, the Commission in *The Crowell-Collier Publishing Co., et al.*, 70 F.T.C. 977 (1966), imposed such a requirement some 10 years ago.[105] The reviewing court expressly approved the requirement although competitors were not so restricted. *P. F. Collier & Son Corp.* v. *FTC*, 427 F.2d, *supra* at 275–76.

A substantial portion of the public prefers not to deal with door-to-door encyclopedia salesmen. Respondents do not affirmatively disclose, at the time of the initial contact with the consumer, that the purpose of the call is to make a sale (Findings 127-29, 132). Respondents' officials feel it is necessary to have a transitional period in the home to set the stage prior to making such disclosure.[106] The purpose of the salesman's call is clearly a material factor in the consumer's decision as to whether to admit the individual at the door. [151]

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[104] Complaint counsel urge that the provision should be adopted in this case because of the difficulty of meeting the conditions prerequisite to payment of the guarantee and the disparity of the income earned and that promised. The differences on this point in the two cases do not appear appreciable. (See *Britannica* Initial Decision, p. 82.)

[105] In that case, the respondent was required to cease and desist from:

> "Failing to disclose at the time admission is sought into the home, office or other establishment of the prospective purchaser or purchaser that the person making the call is respondent's salesman and is soliciting the sale of respondent's merchandise." 70 F.T.C., *supra* at 1033.

The record here, as in *Britannica*, demonstrates that respondents' sales representatives were trained to disguise or misrepresent the main purpose of their visit, which was to sell (Findings 128-30, 132). Consider, for example, the following telephone talk in a sales manual furnished to respondents' sales representatives: [152]

> Hello, Mrs. ________________? My name is ________________and I am calling for the Grolier Society. Does that name mean anything to you? Well, Grolier is the world's leading manufacturer of educational products - however, let me put your mind at ease Mrs. ________________ *I didn't call you to give you a sales talk.* You see Grolier has several new products which they are *testing* right now with several families in each community . . . These new products are used by the children and we want to get some help from these different families and we pay the families for that help in merchandise. Now, due to the unusual nature of this program Grolier insists that it be explained to both husband and wife . . . Grolier will have a member of their staff out in your area this evening . . . He would want to spend about 10 minutes with you and your husband to explain how you can help us . . . *please be sure to tell your husband that he will be there and that he is not coming out to give you a sales talk!*

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[106] Respondents' officials object to disclosing at the door that the purpose of the call is to sell and contend that a card making such a disclosure would be a "very negative thing" (DeLucia 15071). The basic approach today as outlined by one of respondents' Regional Vice Presidents is:

> "Hi, Mr. Jones, my name is . . . . I am doing some work in the area for Grolier Interstate. Do you mind if I step in for a minute. I would like to talk to you" (Tr. 15072).

The problem with the card from respondents' point of view "is not being able to set the stage with regard to explaining to the individual, not at the doorstep, but rather in his home, that I would like to discuss with him some educational products, encyclopedias, after the stage is set" (Tr. 15073). On the other hand, in respondents' view, if the disclosure required by the card was made at the door, *"it would be too easy for that individual to say to me in a very nice way, thats great. We have some"* (emphasis supplied; Tr. 15073). Respondents' officials desire five minutes to set the stage and to do so in the home.

> ". . . If I could have five minutes, of having that individual break down that barrier. . . . If we can get that individual to just sit down, and take a sigh of relief in his home, that I am really not too bad a guy and I would like to just talk to him about Monday night football for a minute before I start going into what I am doing. . . ." (Tr. 15074).

Another of respondents' witnesses testifying on the basis of his long experience in the encyclopedia sales industry stated that the card-at-the-door requirement would have a devastating effect on ability to gain entrance into the home. The objection appears to go as much to the requirement of affirmative disclosure at the door as to the mechanics of the card:

> "I feel that, first of all, there is a great deal of distrust when someone comes to a door nowadays anyway. There has been for a number of years. I believe that if you are to do something quite out of the normal, from what anyone else might do when they go to that particular door, that that just raises some red flags of distrust, concern and wonder why someone would do this. I don't believe that's the place to identify yourself. *I believe you should identify yourself, but I believe it should be when you are able to develop a little bit of rapport* with the customer and sell yourself somewhat and then sit down and be able to explain what you are there for. *You don't try to do this sort of thing on a door step. You do it in their living room* and if they are interested fine; if they are not, fine, too." (Emphasis supplied; Stearns 14625.)

Will you do that? Good. He will see you folks tonight. (Emphasis supplied; CX 563 "O".)

(See also Finding 118.)

The Commission in *Britannica*, on the basis of similar facts, imposed the requirement that, at the time admission is sought to the consumer's premises, the sales representative present a 3 X 5 card showing the names of the corporation and the sales representative, the term "Encyclopedia Sales Representative" or other applicable product, and the terminology "the purpose of this representative's call is to solicit the sale of encyclopedias [or other applicable product]."

The consumer's right to know the purpose of those seeking admission into his home has been firmly established. (See *Crowell-Collier, supra*, n. 105.) The Commission's determination in *Britannica*, that affirmative disclosure in the form of the card-at-the-door requirement is necessary under such circumstances to prevent deception, is binding here. Respondents complain that the imposition of the card-at-the-door requirement would be highly injurious to their business. However, the applicable provision in *Britannica* to be incorporated here is less onerous than the requirement set forth in the notice order.[107] [153] In any event, the assertion of economic hardship may not preclude the imposition of the remedial measures necessary to prevent deception. See *Arthur Murray Studio of Washington, Inc.*, 78 F.T.C. 401, 443 (1972), *aff'd.*, 458 F.2d 622 (5th Cir. 1971.)[108]

Respondents contend that the card-at-the-door remedy would be ineffective since the individual sales representative could not be relied upon to comply with the requirement. They urge that effective measures to counteract deception in in-home selling must not rely on action to be taken by the individual sales representative. The short answer is that, where a firm violates the law through the actions of its sales representatives and is responsible for those actions, the Commission may require that seller to control his sales representatives. This is not a novel principle and it requires no further citation. Moreover, the record in this proceeding shows that, through such techniques as verification calls and telephone surveys, respondents are able to effectively monitor their sales representatives' activities.[109]

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[107] The size of the card has been reduced and the requirement that the customer sign the card before the sales representative gains entry has been eliminated.

[108] The cooling-off period within which a contract may be cancelled may ameliorate the effects of deceptive practices. It is not, however, an acceptable substitute for preventing them in the first instance. *Arthur Murray Studio of Washington, Inc.*, 78 F.T.C., *supra* at 442-43.

Complaint counsel's proposals for the provisions pertaining to the card-at-the-door remedy include some minor departures from the comparable provisions in the *Britannica* order. Specifically, in Paragraphs IID(3), they would add the phrase "when an encyclopedia is not part of the offer" after the requirement that the card use the term "Encyclopedia Sales Representative [or other applicable product]." They propose a similar change for Paragraph IID(4). Complaint counsel state these changes are designed to cover situations where encyclopedias may not be part of the package sold by respondents. They advise in those situations that respondents' salesmen would not be required to disclose that they are encyclopedia [154] sales representatives. There is no need for such changes. Under the *Britannica* order, whose provisions will be incorporated here, if encyclopedias are not sold, the "other products" description would come into play.

The changes proposed in Paragraph IIE for clarification purposes will not be adopted.[110] They neither clarify nor add to the substance of the order.

3. *Order Provisions Pertaining to Pricing Claims and Offers of Free Goods*

Savings claims through the use of terms such as "retail price" and related representations are deceptive when substantial sales of the products in question have not been made at the represented "retail" price. *Guides Against Deceptive Pricing,* 16 C.F.R. 233. Misleading offers of "free" goods may also be prohibited. *Guide Concerning Use Of The Word "Free" And Similar Representations,* 16 C.F.R. 251. Advancing fictitious reasons to make price reduction or "free" representations more plausible has the potential of effectuating purchases which might otherwise not be made. Such practices violate Section 5 of the Federal Trade Commission Act. *Southern States Distributing Co.,* 83 F.T.C. 1126, 1176 (1973).

Respondents' sales representatives were trained and required to sell a combination of products and services at the price established by respondents. The combination or package price established by the respondents was the regular [155] price at which such products were sold (Findings 89, 157–58). The combination price was not a reduction from prices at which substantial sales of such products had been made, and respondents gave no free goods to the consumer. The record demonstrates that respondents have utilized deceptive comparative pricing claims, represented, contrary to fact, that certain goods were free, and advanced fictitious reasons to make more convincing their price-reduction and free-goods representations.[111] These practices will be prohibited.

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[109] Verification has been found to be an efficient way of checking up on what respondents' sales representatives do (DeLucia 15087).

[110] Complaint counsel propose to add the language italicized:

> II-E. Failing to give the card required by and in accordance with the procedures set forth in Paragraph II D above, to each such person, *and at the time such card is given to such person* direct each such person to read the information contained on such card and provide each such person with adequate opportunity to read such card before engaging each such person in any sales solicitation.

The provisions in the *Britannica* order relating to misrepresentation of price reductions and offers of free goods adequately remedy the law violations documented here. They will be adopted in this proceeding. They will be augmented, however, by provisions specifically designed to deal with certain of the fictitious reasons advanced to justify purported offers of price reductions or free goods in return for various forms of help and cooperation on the consumer's part. (See Paragraph IIG6, subparagraphs (d) through (h) of the Order.) [156]

Complaint counsel propose two significant departures from the *Britannica* order which require discussion. They recommend that respondents be prohibited from representing that a price is a regular retail price unless at least 30 percent of their sales for that product have been made at that price or a higher price for the previous six months. Commission counsel acknowledge that the Commission, in *Britannica*, rejected a similar provision which would have required that 40 percent of the sales be made individually before such a representation could be made. They urge, however, that differences in the *Britannica* record and in the record of this proceeding justify the imposition of such a provision. In this case, they argue, it is necessary to define substantial sales with a percentage figure to ensure that the Order is enforceable. They state that this case is distinguishable from *Britannica* since these respondents maintain no records enabling them to calculate the percentage of individual sales at the higher price. Complaint counsel further urge that, when such information was requested in this proceeding, the data was not preserved. These facts, complaint counsel assert, indicate that an order not defining substantial sales would be difficult, if not impossible, to enforce.

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[111] Respondents have represented, contrary to fact, that prices will be reduced or certain merchandise furnished at no cost in return for help provided by the customer in promoting the merchandise or keeping the reference materials up to date (Findings 145, 147–48). In fact, customers were not required to furnish such cooperation as a condition to making such purchases at the combination price (Finding 149).

Another fictitious reason employed by respondents to make the offer of free or bonus goods more plausible was the so-called 10-year conversion plan. In that approach, the price was first stated in terms of payments over a 10-year period. The customer was then offered free goods or merchandise at no extra cost for paying off the contract in approximately three years on the ground that the shorter payment period would benefit respondents by reducing the collection costs (Finding 173).

The argument will be rejected. As in *Britannica*, respondents will be required to maintain adequate records to substantiate the validity of their pricing claims. There is no reason, accordingly, to depart from the Commission's determination in *Britannica* that orders in this area should not vary from the Commission's *Guides Against Deceptive Pricing*, 16 C.F.R. 233. In the *Britannica* order, the pricing provisions were expressly conformed to that provision in the Guides stating that the retail price may be described as a selling price if "substantial" sales are made at the retail level (*Britannica, supra* at 9). That precedent will be followed here.

The failure to maintain records to substantiate respondents' pricing claims, however, warrants relief.[112] The consumer [157] is entitled as a matter of marketplace fairness to rely upon the seller to have a reasonable basis for such representations. Cf. *Pfizer Inc.*, 81 F.T.C. 23, 62 (1972); *The Firestone Tire and Rubber Co.*, 81 F.T.C. 398 (1972, *aff'd.*, 481 F.2d 246 (6th Cir. 1973), *cert. denied*, 414 U.S. 1112 (1973). Sales made on the basis of unsupported claims, moreover, are unfair to competitors as well as consumers. The Guides Against Deceptive Pricing impose a requirement that a seller be "reasonably certain" that his pricing claims are correct. 16 C.F.R. 233. It is unfair to make pricing claims without supporting data to document their accuracy. Respondents will be prohibited from making pricing claims unless they have records from the preceding six months to document the validity of such representations.

The other significant departure from the *Britannica* order proposed by complaint counsel pertains to the use made by respondents of cost figures relating to the Information Service.[113] In this connection, respondents have utilized certain figures as the cost to the company of furnishing an answer to a request for information, for example, $3.32. Respondents have represented to consumers that the total cost or liability to them for furnishing 100 answers over a 10-year period would be in excess of $300 (Findings 154, 165). Complaint counsel apparently do not challenge the accuracy of the cost figures[114] as such, but maintain that the use of such figures in connection with the retail prices or values for other items in the combination is inherently deceptive. They contend it builds up the claimed retail value of the combination in a misleading way.

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[112] ". . . The books and records of Grolier and its subsidiaries are not maintained in such manner as to set forth the numbers of each product or service sold separately or the total dollar sales of such products or services sold separately. . . ." (Respondents' Special Report In Response To Order Of March 13, 1970, CX 5N.) In short, respondents were unable to document that the retail, list or individual price of the product was the usual or regular price of such product at which it was sold in substantial quantities.

[113] The Service is also sometimes referred to in the record as the Fact Research Service.

[114] See Tr. 10789.

The use of cost figures for the Research Service in conjunction with retail prices or values for other items in the combination has the capacity to mislead. The use of noncomparable figures (the Research Service is never sold at retail) to build up the claimed retail value and inflate asserted price reductions should be prohibited. However, complaint counsel's proposal would prohibit any use of cost figures in connection with the Information Service. There is insufficient evidence [158] to make a finding that such figures are inaccurate. The Order should not be framed so as to preclude a legitimate use of such figures. Complaint counsel's proposal will be revised. Respondents will be required to cease and desist from representing, directly or indirectly, that:

> (d) any research service is being offered at any price or that the research service has a retail value unless such is the fact;
> (e) the cost to any respondent of any research service represents a retail value.

(Paragraph II I (d)-(e).)

4. *Order Provisions Pertaining to Representations of Terms, Conditions, Method, Rate or Time of Payment*

Paragraph II-H of the Order proposed by the Commission staff would prohibit respondents from:

> H. Making any reference or statement concerning "10 cent per day," "10 years," or any other statement as to a sum of money or duration or period of time in connection with a sales contract or any other agreement which does not in fact provide, at the option of the purchaser, renter, or lessee, for the payment of the stated sum, at the stated interval, and over the stated duration or period of time; or misrepresenting, in any manner, the terms, conditions, method, rate or time of payment actually made available to any person.

The record shows that respondents' sales representatives have, at least impliedly, represented that 10-year payment plans were available and, in order to minimize the price, have prorated the payment in cents per day over such 10-year period. In fact, a 10-year payment plan was generally not available and most sales representatives were not authorized to offer such a plan (Findings 170, 174). Clearly, the misrepresentation of the time period within which payment could be made was deceptive. Equally deceptive was the allied misrepresentation prorating the price in terms of cents a day over a time period having no relationship to the payment plan actually available. Such [159] practices deceptively minimize the price which the consumer must pay and should be prohibited. On the other hand, there is insufficient evidence in this record to support a finding that cents-a-day representations pertaining to a time period in a payment plan actually available are either inherently deceptive or unfair. No precedent has been cited to support such a position. The record would not sustain a finding that a cents-a-day representation, standing alone, has the capacity to mislead consumers into the belief that they could actually make payment on a cents-a-day basis. In short, a blanket prohibition on such representations does not appear justified. The provision will be modified to prohibit:

> Misrepresenting, in any manner, the terms, conditions, method, rate or time of payment actually made available to any person.

(Paragraph II-H.)

5. *Proposed Order Provisions Relating to Notice of Violations and Restitution*

Complaint counsel propose that respondents be required to furnish their customers with a notice summarizing the selling provisions of the Order. They urge that this proposal would create a mechanism enabling the Commission to monitor compliance with the Order and to take such actions as are necessary to redress consumer complaints. Such a provision was not included in the *Britannica* order. Complaint counsel urge, however, that the facts presented in this case justify inclusion of the provision. Complaint counsel propose a further provision that respondents be required to refund to purchasers all monies paid if purchasers can demonstrate that the sales transaction involved was a violation of the Order. A provision of this type was neither sought nor included in the *Britannica* order.

Turning first to the provision which would require respondents to notify consumers of the violations within the scope of the Order, it is apparent that, as a general rule, the Commission has refused to impose such consumer-warning requirements even where fraud is the essence of the practice as in the case of bait and switch representations. See *Maryland Carpet Outlet, Inc.*, 3 CCH Trade Reg. Rep. ¶20,906 (1975 [85 F.T.C. 754]). There are no facts apparent on the face of this record supporting a departure from that precedent in this case. [160]

The efficacy of the restitution provision suggested by complaint counsel depends to a considerable degree upon the related proposal of a consumer warning provision which will not be adopted for the reasons stated. Complaint counsel argue for inclusion of this proposal on the ground that previous Commission enforcement proceedings with respect to the respondents in this case have been ineffective in the past. There is no persuasive showing that there are significant differences between the respondents in *Britannica* and this proceeding in this respect. No convincing arguments have been advanced to sustain a departure from so recent a precedent placing the respondents herein at a disadvantage with respect to a major competitor.

6. *Order Provisions Relating To Respondents' Solicitation of Leads Through Schools*

Respondents have sent materials through the schools to homes of students designed to secure entry to such homes for the purpose of making sales presentations. The record shows that respondents have persuaded school officials to permit the dissemination of such materials without disclosing to such officials that they intended to follow up with sales presentations. The record shows that respondents have disguised to school officials the purpose of disseminating their promotional materials through the schools which was to secure leads for in-home sales presentations (Findings 92–96). This method of transmitting promotional materials has the capacity to mislead parents into the belief that the school is endorsing such products and respondents' selling efforts (Finding 98). Respondents have, on occasion, reinforced this impression in the case of parochial schools by sending the materials home in a large envelope imprinted with a cross (Finding 97).

The record justifies the imposition of affirmative disclosure requirements to prevent the repetition of such practices. Complaint counsel's proposed order on this point, however, is unduly lengthy and cumbersome. The proposal will be revised so as to require disclosure to school officials that the purpose of disseminating such materials is to secure leads in order to facilitate in-home sales presentations. The Order will also require a disclosure on the face of such materials that their dissemination through the school does not constitute an endorsement or a recommendation by the school or its officials that such materials be purchased unless, in [161] fact, such an endorsement has been given or such a recommendation made[115] (Paragraph IIL).

The issuance of the Order provisions directed to these practices, complies with the requirements of due process even though they were not included in the provisions of the notice order. The practices to which these provisions relate were clearly in issue during the trial of the case. The Commission, moreover, is not bound to rigidly adhere to the provisions of the notice order if the record indicates that it should be modified. As the notice order states, its provisions are subject to change if the facts developed during the adjudicative proceeding indicate that such provisions might not be fully adequate to protect the consuming public.

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[115] The provisions of Paragraph IIA and B of the Order will require the disclosure to parents, on the face of such promotional materials, that they may be contacted for the purpose of a sales presentation.

7. *Order Provisions Designed To Prevent False Emotional Appeals*

Complaint counsel contend that respondents created such programs as "The Child Development Program," "The National Institute of Programmed Learning," and "The Mothers Club" to appeal to the emotional concerns of parents for the proper education of their children or their own intellectual development. They urge that the essence of such a program is to make the prospects believe that respondents are offering something substantially different from just encyclopedias, and that parents are made to believe that such assistance, over and above that provided in the school, is required to properly educate their child. They further contend that the record shows that parents are purposely made to feel guilty if they do not accept this offer. In support of this contention, they also rely on evidence that, in a presentation designed for the Spanish-speaking population, respondents utilize a "Technique of a Threatening Eventuality" implying that their reference materials are a prerequisite to success (CX 2278). [162]

To prevent appeals of this nature, complaint counsel propose to prohibit the following practices:

> Y. Using the words "Child Development Program," "Mothers' Club," "National Institute of Programmed Learning" or words of similar import and meaning to represent, directly or by implication, the existence of a *bona fide* educational program, club or business entity which provides educational services or benefits to consumers.
>
> Z. Using any promotional device, program or representation which falsely or unfairly appeals to the concerns of individuals for their own educational or intellectual development or of parents or prospective parents for the proper educational development of their children; or using any promotional device, program or representation to confuse, confound or obfuscate the actual purpose of the promotional device or program which is to attempt to promote the sale, rental or lease of publications, merchandise or services.

The record shows that respondents have used devices, such as the "Mothers Club," to imply the existence of a bona fide educational club program or business entity which provide educational services or benefits to customers.[116] In fact, they were simply devices to sell respondents' products (Finding 122).

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[116] For example, representations were made in connection with the "Mothers Club" that the sales representatives were "field counselors" and that the consumer was being "enrolled" in the Club (Findings 123-25, 129, 151).

The use of trade names implying that a business is something other than a commercial enterprise is unfair. *Mather Hearing Aid Distributors, Inc.,* 78 F.T.C. 709, 735 (1971). The courts have uniformly sustained orders prohibiting the use of designations misrepresenting the nature of a respondents' business. *Goodman* v. *FTC,* 244 F.2d 584, 595 (9th Cir. 1957). **[163]**

Such practices can be enjoined and respondents will be prohibited from using names, such as the "Mothers Club," implying the existence of a genuine educational club or program in connection with their sales presentation or offers of sale.

The provision designed to enjoin false emotional appeals is another matter. The Commission simply cannot enjoin every promotional ploy as, for example, the "Threatening Technique" which may be in poor taste or unfair. Complaint counsel's proposal on this point is too vague to be enforceable. If a practice is to be prohibited, it must be capable of clear definition, otherwise the provision designed to curb such practices becomes excessively vague. It is not practical to frame an order prohibiting practices such as appeals to parents' feelings of guilt or to unfair appeals to concern for the educational development of an individual or that individual's child. As the Commission noted in *Arthur Murray Studio of Washington, Inc., et al.,* 78 F.T.C., *supra* at 441, an order prohibiting "generally the use of excessive or unfair pressure would be virtually impossible to enforce." The practices under consideration will be effectively curbed by enjoining the use of names which disguise the purpose of respondents, which is to sell.

8. *Order Provisions Relating to Endorsements*

The use of fictitious or unauthorized endorsements or testimonials is an unfair and deceptive act or practice within the meaning of the Federal Trade Commission Act. *FTC* v. *Standard Education Society,* 302 U.S. 112 (1937). Where such violations have occurred, the Commission, in addition to prohibiting such practices, may require that, before endorsements are used, respondents obtain express authorization in writing for such use. *National Dynamics Corporation,* 82 F.T.C. 488, 565-66 (1973), *modified on other grounds,* 492 F.2d 1333 (D.C. Cir. 1974). Additionally, respondents may be required to have good reason to believe, at the time such endorsements are used, that the person or organization named as endorsing the product currently subscribes to the facts and opinions contained in such endorsement *(id.).* Respondents will also be required to specify the year of the edition of their publications to which an endorsement or testimonial letter pertains. This provision is directed to the practice of using an undated **[164]** endorsement or testimonial letter in conjunction with editions published years after such letter had been written. In a related provision, respondents will be prohibited from representing in any manner that an endorsement has been recently executed or is current unless this is the fact.

9. *Order Provisions Relating to Debt Collection Procedures*

The resort to misrepresentation to collect delinquent accounts has long been considered actionable under the Federal Trade Commission Act. Practices to be prohibited include the false representation that a debt has been turned over to a third party for collection and misrepresenting that legal action will be taken if the debt is not paid. There is a clear public interest in prohibiting such practices. See *S. Dean Slough* v. *FTC*, 396 F.2d 870 (5th Cir. 1968), *cert. denied*, 393 U.S. 980 (1968). Much of the evidentiary record in this case going to the debt collection issue relates essentially to these and related representations.

Respondents have misrepresented that letters emanate from the Legal Departments of their local offices when no such departments exist[117] (Findings 240–43). Respondents will be prohibited from representing that any company, corporation or entity engaged in debt collection has a separate bona fide department or division for legal matters unless those are the facts, or "misrepresenting in any manner, the existence, or functions of any division or department of any company, corporation or entity."

Respondents have used forms implying threats of dismissal from the Civil Service and criminal prosecution for mail fraud as a collection technique in the case of certain of their delinquent accounts. The use of such forms is misleading and unfair; as a general rule, respondents' debtors would not be subject to such sanctions (Findings 262–65). The routine use of forms making such threats should be prohibited. The provision recommended by complaint counsel enjoining the use [165] of such threats unless respondents have sufficient facts to establish the propriety of such a claim in a particular case will be adopted.

Respondents have also sent out forms threatening that a credit reporting agency would disseminate adverse credit reports with respect to a delinquent account when, in fact, no such reports were disseminated (Findings 260–61). That practice will also be enjoined.

Respondents have utilized a number of techniques to directly or indirectly threaten the institution of suit or legal process when no decision had been made to initiate such measures at the time that such representations were made. Respondents have made widespread use of form letters going out under attorneys' letterheads when such attorneys had not prepared or originated the letters, reviewed the account, or been authorized to take any action in connection therewith (Findings 245-52). Under these circumstances, there is no bona fide referral of the account to a lawyer for collection. The existence of this practice also supports a ban on representing that an account has been transferred to any person or entity for purposes of collection unless that is the fact. In addition, respondents have used forms simulating or depicting legal process which had no relationship to actual proceedings to recover any debt (Finding 254).

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[117] The allegation that respondents have misrepresented the existence of separate credit and collection departments has not been established. The mere fact that accounts are transferred from one unit to another, in respondents' local offices, on a predetermined schedule is insufficient to establish that they are not separate departments as complaint counsel contend (Finding 244).

The basic policy of respondents, which is of long standing, has been not to sue delinquent accounts, and the filing of suit is an exception to the general policy (Finding 255). The record further shows that, to the extent that delinquent accounts were ultimately turned over by a headquarters office to third parties such as credit and collection companies or attorneys, that decision had no relationship to the form letters used by local offices making such representations. Similarly, to the extent that a decision was ultimately made in a headquarters office to file suit, that decision had no relationship to the routine use of forms by respondents' local offices making such a threat (Finding 258, n. 80). If suit was, in fact, filed, with few exceptions, such process was not instituted by the lawyers who had lent their letterheads to be used in respondents' "attorney letters."

Respondents will be enjoined from representing that suit will be instituted to recover any delinquent debt, that any delinquent debt will be transferred to any attorney with instructions to institute suit, or that any other legal step to [166] collect any outstanding debt will be taken, unless a definite date is set for such act and such are the facts. The record further justifies a prohibition on misrepresenting in any way respondents' relationship with, or instructions to, any attorney, or the course of action that will be taken by any lawyer. These provisions in the *Britannica* order will be applied here. Respondents' use of forms to depict or simulate legal process will similarly be prohibited.

10. *Order Provisions Relating to Continuity Programs*

Respondents' advertisements and promotional materials soliciting participation in their continuity program, prior to March 1971, created the impression that all the books in the series would be shipped singly at intervals of approximately a month. Such promotional materials failed to disclose that all but the first few volumes in the series would be sent in a bulk shipment (Finding 230). Many customers have a preference for receiving such books singly and the failure to disclose, in the initial customer contact, that they would receive a bulk shipment constituted the failure to disclose a material fact (Finding 231).

Respondents have also represented that persons joining or participating in such programs do so at no risk or obligation. However, participating in such continuity programs did entail certain risks and obligations. Consumers were subject to the risk of receiving a bulk shipment if the negative option provided by respondents was not successfully exercised. If books were not wanted, the consumer had to reject them and do so within the allotted time. If a timely notice of cancellation was not received due to delays in the mail, they risked being billed for publications even after such publications had been returned (Findings 234–36).

The foregoing practices are essentially identical to those found illegal in *Britannica*. The provisions in the Order issued in that proceeding will be entered here. The provisions in the *Britannica* order to be adopted in this proceeding will prohibit misrepresentations that (1) a person has the option to receive each publication separately and individually and reject the same; (2) that a person will not receive further merchandise after respondent has received a timely notice of cancellation unless that is the fact; and (3) that no risks or obligations [167] are incurred in joining or participating in the program or misrepresenting in any manner the rights, duties or obligations imposed thereunder (Par. IIIA). In their advertising, respondents will be required to describe the conditions and terms of their continuity programs, the method of sales or distribution and the subscriber risks and obligations. Respondents will also be required to describe in their advertising the merchandise or products offered, the billing charges, the anticipated total number of publications, the number of publications to be included in such shipments and the intervals between shipments (Par. IIIB). The Order further requires that on each return coupon, order form or similar document, respondents will be required to disclose the following: the anticipated total number of publications, merchandise or services included in the program; the number of publications to be included in each shipment; and the number of and intervals between each shipment (Par. IIIC). In addition, respondents will be required to affirmatively disclose in connection with any shipment or notice thereof, the anticipated date on which respondents will initiate the processing of the next shipment (Par. IIID). Finally, the Order requires that respondents disclose in each notice of shipment, the means by which a person may exercise his option or right to cancel such shipment if that is his right (Par. IIIE).

The foregoing provisions appear ample to correct the law violations documented in this proceeding. Complaint counsel, however, urge that additional provisions to clarify the consumer's risks and obligations and to spell out more clearly the procedures with respect to cancellation and returns also be adopted. (See Proposed Order IIIB(3) and (4), IIIE, IIIG and IIIH.) These provisions will not be included in the Order. They do little more than amplify the provisions in the *Britannica* order addressing themselves to the question of representations concerning the consumers' risks and obligations and the disclosure requirements pertaining to the operation of the program. The additional provisions are of marginal value and whatever benefit they may have is outweighed by the fact that they would complicate both enforcement and compliance with the Order. It is not practical for Commission orders to provide for every conceivable contingency. Cf. *Bantam Books, Inc.* v. *FTC*, 275 F.2d 680 (2d Cir. 1960), *cert. denied*, 364 U.S. 819. Moreover, there do not appear to be significant differences between this proceeding and *Britannica* justifying [168] the inclusion of these proposals.[118]

11. *Order Provisions Relating to Cooling-Off Period*

The Order herein will incorporate the provisions of the Commission's Trade Regulation Rule, *Cooling-Off Period For Door-To-Door Sales*, 16 C.F.R. 429.1 The reasoning in *Britannica*, that this provision is required to provide relief from sales practices of the nature under consideration here, applies to this proceeding.

12. *Proposed Order Provisions Relating to Quality of Product*

Complaint counsel also propose a prohibition to prevent respondents from using prospectuses or sample volumes in their sales presentations "not representative in kind and quality of each volume included in such set of publications" (Proposed Order IIG).

The quality issue as such was not expressly alleged in the complaint. This issue came into the proceeding as an afterthought and the evidence on this point is sketchy. In complaint counsel's memorandum outlining their position as to the relevance of this evidence,[119] complaint counsel made it clear that such evidence should go to the limited question of remedy and specifically to the length of the cooling-off period. They asserted such evidence was relevant to the question of whether the cooling-off period should be extended subsequent to the time the products had been received. Complaint counsel urged that merely prohibiting quality misrepresentations would be insufficient. Under these circumstances, it does not appear that a prohibition unrelated to the cooling-off period should be entered. [169]

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[118] See the findings in *Britannica* that some customers were subjected to unrelenting mailings of bills and dunning letters demanding payment for books that had been previously returned or never received and that continuity customers had even received shipments of books after they had cancelled the program (Initial Decision, p. 100).

13. *Proposed Order Provisions Requiring Respondents To Conduct Surveillance of Sales Activities*

The Order proposed by the Commission staff, like the order entered in *Britannica*, requires respondents to provide copies of the order to any person engaged in the sale, promotion, or distribution of their products. Those provisions will be adopted here. In addition, complaint counsel propose that respondents be required to institute a program of surveillance to determine whether those they have engaged to sell their products have complied with the order. Respondents under this proposal would be required to terminate those violating the order if such violations involve two or more customers or prospects during a six-month period. The proposed surveillance provisions would cover respondents' own sales representatives as well as their outside distributors.

The proposal that respondents be required to institute a surveillance program over their sales representatives was rejected in *Britannica*. It was rejected as unnecessary because of the increase in civil penalties for violations of Commission orders. Complaint counsel urge a different result should be reached in this proceeding. They contend that these respondents have historically used a wide variety of sales presentations and recruiting practices in contrast to the uniformity and centralized control characteristic of the Britannica operation. As a result, they assert a surveillance program is required to detect and eliminiate violations of the order. The provision will not be entered; respondents herein have moved to centralize control. The prospective penalties for violations should be a sufficient inducement to spur respondents to take the steps necessary to ensure compliance.

The proposal that respondents be required to monitor the activities of their outside distributors raises a number of issues not considered in *Britannica*. Complaint counsel urge that respondents be required to institute a program of surveillance in the case of distributors when respondents direct, control or approve their promotional practices, provide promotional materials or aids, or finance at least 40 percent of the contracts procured by such persons or entities. [170]

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[119] Memorandum Outlining Complaint Counsel's Position On The Quality Of Respondents' Products And Services As An Issue In This Case, dated June 10, 1975.

Citing cases such as *FTC* v. *National Lead Co.*,[120] complaint counsel urge that such a provision is well within the Commission's power to require affirmative action to cure the effects of illegal conduct and to prevent its recurrence. The Commission's general powers to require affirmative action to achieve effective relief are not in issue. The question is whether requiring such surveillance can be justified on the basis of the facts presented in this proceeding.

Complaint counsel state that the proposed order does not seek to hold respondents directly liable for the acts and practices of their distributors. Rather, the provision under consideration is designed to ensure that respondents will not be permitted to do indirectly through distributors what the Order forbids them to do directly. Citing cases such as *International Art Co.* v. *FTC*,[121] *Permanent Stainless Steel, Inc.*,[122] and *Star Office Supply*.[123] Complaint counsel urge that the Commission has frequently imposed liability on manufacturers for misleading sales representations by persons who were independent contractors rather than its agents or employees.

Complaint counsel contend it is unnecessary to find respondents vicariously or directly liable for the acts of their distributors to sustain the proposed surveillance provision. (Complaint Counsel's Brief, p. 55, Complaint Counsel's Answering Brief, p. 58.) Moreover, they expressly disavow reliance upon the acts and practices of such distributors to establish liability on the part of respondents.[124]

The argument is not entirely clear. Complaint counsel appear to concede that there must be at least some showing of liability on respondents' part before such an order can be sustained. They state: [171]

> . . . However, the basic principle underlying both the imposition of direct liability and a surveillance provision is the same - that is that a respondents' relationship to persons who sell its products is such that is appropriate that the respondent be held responsible for the actions of said parties. Thus, we submit that the same factors,

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[120] 352 U.S. 419 (1957).

[121] 109 F.2d 393, 396 (7th Cir. 1940).

[122] 51 F.T.C. 734, 745–46 (1955).

[123] 77 F.T.C. 383 (1970), *aff'd*, 1972, Trade Cases ¶73,867 (2d Cir. 1971), *cert. denied*, 92 S. Ct. 1767 (1972).

[124] ". . . we do not rely upon the acts and practices of Jayhill or the Richards distributors to establish respondents' liability. We submit that it is not necessary to find that either Grolier, Incorporated or Richards are vicariously liable for the acts of the distributors in order to sustain the proposed order. . . ." (Complaint Counsel's Brief, p. 55).

which are considered in determining the direct liability of respondents for the acts of other parties are relevant in considering whether a surveillance and termination provision is appropriate. . . .

Complaint counsel evidently rely on that line of cases finding liability where sales persons-independent contractors act within the scope of apparent authority conferred by the manufacturer,[125] the manufacturer has placed in the hands of others the instrumentality of deceit[126] or the interrelationship between the manufacturer and its independent sales representatives was so pervasive that respondents materially contributed to and participated in such activities for their own benefit.[127] The Commission is not bound by the common law rules governing vicarious liability or agency.[128] Nevertheless, it is also clear that a seller does not become amenable to Commission process for all sales further down the chain of distribution absent a showing of responsibility for, or involvement in, the activities of those reselling his product. [172]

If the order sought is to be entered, there must be a showing that (1) respondents directed or controlled their distributors' sales or recruiting practices; or (2) the materials furnished by respondents placed in the hands of their distributors the means of deception; or (3) the distributors' sales or recruiting activities are within at least the scope of apparent authority conferred by respondents. Absent a showing that at least one of these criteria has been met, the surveillance requirement cannot be justified. The record demonstrates no control by respondents in the case of distributors not financed by them which would justify the imposition of an order requiring surveillance over the sales or recruiting practices of such retailers. The record, moreover, contains no information as to the nature of the sales and recruiting practices of distributors in this category.

The question is closer in the case of the Richards' spin-off distributors and the former Jayhill-Hemphill operation. The Jayhill-Hemphill operation, however, no longer exists.[129] The question will be resolved on the basis of the evidence pertaining to the Richards' spin-off distributors whose contracts have been financed by Bunker Hill, a subsidiary of respondent Richards.

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[125] *Goodman* v. *FTC, supra.*

[126] *FTC* v. *Winsted Hosiery Co.*, 258 U.S. 483 (1922).

[127] In *Star Office Supply Co.*, 77 F.T.C., *supra* at 445, the Commission held:

> ". . . Respondents sought to benefit from the wrongful acts of the jobbers, fully knowing the nature, purpose and result of those acts. By supplying the financial backing, the inventory, the physical facilities, the clerical services, shipping—in fact all elements of the scheme except actually taking the customers' orders—the respondents materially and substantially contributed to, and participated in, the salesmen's activities for their own benefit."

[128] See *Goodman* v. *FTC, supra; Permanent Stainless Steel*, 51 F.T.C. 734, 745 (1955).

[129] In the case of the Jayhill-Hemphill operations, the standard of control and apparent authority may have been satisfied (Findings 269-72).

Considering the record as a whole, the evidence bearing on the question of whether respondents are responsible and liable for the actions of the spin-off distributors is subject to conflicting inferences (Findings 273-88). By and large, however, the contacts between respondents' officials and these distributors are not inconsistent with a finding that they were normal business communications such as may be expected of any manufacturer and his outside retailers. On balance, the evidence does not sustain a finding that respondents controlled or are responsible for the actions of such distributors. [173]

It is, however, unnecessary to reach the question of whether respondents are liable for the actions of these distributors. The proposed surveillance remedy is inherently inappropriate for a number of reasons. The surveillance procedure to prevent indirect violations of the Order is unnecessary. The criteria for holding a respondent liable for the actions of his independent contractor-sales representatives (or distributors) have been clearly spelled out by precedents such as *Permanent Stainless Steel, Inc.*, 51 F.T.C. 734 (1955), *Goodman* v. *FTC, supra*, or *Star Office Supply Co., supra*. If respondents' relationship with their distributors is such as to bring them within that line of decisions, then this Order will cover the unfair practices, if any, committed by such distributors.[130] On the other hand, if the criteria in those cases are not met, then an order requiring the surveillance procedure would not be justified in any event.

The surveillance provisions by virtue of the burdens imposed would tend to discourage respondents from seeking new avenues of distribution. In that respect, the effect would be punitive. Enforcement efforts might be eased if respondents were to refrain from expanding their sales effort through distributors. It is not, however, the purpose of cease and desist orders to freeze a respondent's method of distribution with the resultant risk of inefficiency.

Finally, the parties appear to agree that the distributors under consideration are independent and separate entities. The record indicates that such distributors, as retailers of respondents' encyclopedias in combination with other products, of necessity, compete with Grolier Interstate's [174] nationwide in-home selling operation.[131] The fact that such distributors are also respondents' actual or potential competitors is a crucial factor in the consideration of remedy. In addition, these distributors, as a practical matter, are respondents' customers.[132] The possibility of vertical and horizontal restraints resulting from the proposed surveillance procedure should not be ignored.

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[130] The standard provision in Commission cease and desist orders prohibiting violations by respondents' employees, agents, and representatives, directly or through any corporate or other device, also contained in this Order, would cover indirect violations by respondents through their distributor network. It would only be necessary to demonstrate within the meaning of the precedents that respondents' relationship with their distributors was such that they should be held liable for their acts.

The advisability of requiring respondents to institute such surveillance procedures over firms who buy from and are actual or potential competitors of the Grolier companies is questionable. Consideration must be given to the antitrust implications of such a provision. When weighing such remedies, the possibility of trade restraints impairing price competition or impairing a competitor's ability to gain access to certain markets cannot be ignored. *E.g.*, see *Hummel Antitrust Problems Of Industry Codes Of Advertising, Standarization, And Seals Of Approval*, XIII Antitrust Bulletin 607 (1968).

There is also the danger that such surveillance and concomitant communications between respondents and their distributors would result in the blacklisting of various employees. It is one thing for an employer to terminate a misbehaving sales representative; it is another to subject such decisions to possible agreement or discussion between competitors.[133] [175]

There is, moreover, a danger of abuse when businessmen police the activities of their competitors, particularly where there is inequality of economic power. Cf. *Silver* v. *New York Stock Exchange*, 373 U.S. 341, 359 (1963). And, even where self-regulation is mandated by statute, such activities have no blanket immunity from the antitrust laws (*id.* at 359-60). Law enforcement is a governmental function which should be left with the agency to which it has been entrusted by statute. The regulatory powers of government should not be turned over to even well-intentioned private parties. (Cf. Dissent of

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[131] The record shows in the case of one distributor that he and Grolier Interstate competed both in the hiring of sales representatives and in selling to consumers (Pardee 11098).

[132] The jobbers, from whom the financed distributors ostensibly buy at cost, make their profits on such transactions only on the basis of the amounts retained from collections. The goods, moreover, are dropshipped by respondents' subsidiary to the customer. Under the circumstances, the jobber appears to be essentially a conduit between respondents' subsidiaries and these distributors.

[133] Compare the holding of the Commission in *Federal Trade Commission Advisory Opinion On Selling Code For Paid-During Service Periodical Subecription Sales Agencies*, 307 ATTR X-1 (1967):

> ". . . the Commission is unable to give its approval to those sections of the Code which apply to the salesmen as those sections are now written. While the Code now provides that the action to be taken with respect to the salesmen found to be in violation would be on the basis of a recommendation by the Administrator rather than by agreement among the signatory agencies, the Commission believes the probable result of that recommendation would be to substantially interfere with those individuals' right of employment and their right to have their fate decided by their individual employers uninfluenced by virtually mandatory recommendations from the Administrator."

Commissioner Elman, FTC *Advisory Opinion On Selling Code For Paid-During Service Periodical Subscription Sales Agencies, supra,* n. 133). Efforts to improve advertising and selling practices should proceed in ways that contribute to competition rather than to impede it. (See *Hummell, supra.*) In short, the probable antitrust dangers of this remedy, in the case of outside distributors, outweigh the possible consumer protection benefits of requiring respondents to conduct such surveillance. This is a critical consideration militating against the imposition of the surveillance provision.

There appears to be a more appropriate alternative to protect the public in this area. Under Section 205 of the Federal Trade Commission Improvement Act, orders may be enforced against nonparties provided they have notice thereof. Under the terms of the Order, respondents' distributors will be furnished with a copy thereof. Respondents will, on a quarterly basis, be required to submit to the Commission, a list of those distributors whose retail installment contracts have been financed by them or any of their subsidiaries or affiliates. With that information, the Commission will be in a position to conduct such investigation as may be appropriate. [176]

CONCLUSIONS

1. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents Grolier, Incorporated, American Peoples Press, Inc., Americana Interstate Corporation, Career Institute, Inc., Grolier Enterprises, Inc., Grolier Reading Programs, Inc., Americana Corporation, Spencer International Press, Inc., The Grolier Society, Inc., R. H. Hinkley Company, Grolier New Era Corporation, The Richards Company, Inc., Madison Enterprises, Inc., Grolier Interstate, Inc., and Federated Credit Corporation.
2. The proceeding is in the public interest.
3. The aforesaid acts and practices of respondents, as herein found, were and are all to the prejudice and injury of the public and of respondents' competitors and constituted, and now constitute, unfair and deceptive acts and practices and unfair methods of competition, in commerce, within the intent and meaning of the Federal Trade Commission Act. [177]

ORDER

I

It is ordered, That respondents Grolier, Incorporated, Americana

Corporation, Grolier Interstate, Inc., Grolier New Era Corp., Madison Enterprises, Inc., R. H. Hinkley Company, The Grolier Society, Inc., Spencer International Press, Inc., and The Richards Company, Inc., corporations, and their successors, assigns, officers, agents, representatives and employees, directly or indirectly, through any corporation, subsidiary, division or other device, in connection with the recruitment, training, or orientation of any person to sell, rent, lease, or distribute any textbook, encyclopedia, reference or educational material, training course or teaching machine, or any other publication, merchandise or service, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

A. Representing, directly or by implication, either orally or in writing, that:

(1) any respondent is offering positions in such fields as advertising, education, public relations, marketing, interviewing, or in any field other than door-to-door [178] sales, if door-to-door sales is included, to any extent, in the position for which persons are being recruited; or misrepresenting, in any manner, the job for which any person is being solicited;

(2) persons will be trained as management trainees, or for other positions of responsibility concerned with administrative office functions, unless, in fact, a formal management training program is available to persons accepting employment on the basis of such representations; or misrepresenting, in any manner, the amount and type of training that will be given;

(3) any person who may be employed will contact prospects in their homes or places of business for the purposes of conducting surveys, advertising promotions, educational instruction or other nonselling functions; or misrepresenting, in any manner, the purposes for which any person is engaged. [179]

B. Misrepresenting, in any manner, the amount of income to be earned by any person or that may be earned by any person, the method of payment, or any condition or limitation imposed upon the compensation of any person, or the degree of ease or difficulty in performing any said condition imposed.

C. Failing to disclose, clearly and conspicuously, in all advertising offering employment in any way involving door-to-door sales:

(1) that the respondent concerned is recruiting persons for the sole purpose of soliciting or selling;

(2) that such soliciting or selling will be on an "in home" basis;

(3) that the products or services being sold are encyclopedias or services to be used in connection therewith, or in the event that

encyclopedias or such related services are not being sold, the products and services being sold; and

(4) the basis for compensating persons so engaged. [180]

D. Failing to clearly and conspicuously advise, both orally and in writing, any prospective salesperson at the initial face-to-face interview, and prior to executing any employment agreement with any such person, the following information:

(1) all those disclosures set forth in Paragraph I C above;

(2) a complete and detailed description of each condition and limitation imposed upon the receipt of any compensation;

(3) where applicable, notification that such person will not be paid for time spent during orientation and training;

(4) a complete and detailed description of any expense or expenses any such person may incur in performing the required duties; and

(5) the percentage of persons holding similar positions engaged by the office offering the position during the twelve (12) months immediately preceding the offer, who have actually received an equivalent, or greater, income than that promised under the terms of any such agreement. [181]

E. Failing to furnish to each applicant at the initial face-to-face interview and prior to executing any employment agreement with any such person, a copy of Paragraphs I, II and V of this order together with a cover letter as set forth in *Appendix A* attached hereto.

F. Making, distributing or using any training tapes, sales manuals, or any other document, method or device which contains any representation or instruction inconsistent with any provision of Paragraph I or Paragraph II of this order.

II

It is ordered, That respondents Grolier, Incorporated, Americana Corporation, Grolier Interstate, Inc., Grolier New Era Corp., Madison Enterprises, Inc., R. H. Hinkley Company, The Grolier Society, Inc., Spencer International Press, Inc., and The Richards Company, Inc., corporations and their successors, assigns, officers, agents, representatives, and employees, directly or indirectly, through any corporation, subsidiary, division or other device, in connection with the publishing, advertising, offering for sale, sale, rental, lease or distribution of any textbook, encyclopedia, reference or educational material, training course or teaching machine, [182] or any other publication, merchandise or service, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

A. Disseminating or causing to be disseminated, any advertisement or promotional material which solicits participation in any contest, drawing or sweepstakes, or solicits any response to any offer of merchandise, service or information unless any such solicitation clearly and conspicuously discloses the following statement in 10-point boldface type:

> *NOTICE TO CONSUMER* - PERSONS WHO REPLY AS REQUESTED MAY BE CONTACTED BY A SALESPERSON FOR THE PURPOSE OF SELLING [insert name of applicable product].

B. Providing any return card, coupon or other device which is used to respond to any advertisement or promotional material covered by Paragraph II A above, unless the following statement clearly and conspicuously appears in 10-point boldface type in immediate proximity to the space provided for a signature or other identification of the responding party: [183]

NOTICE TO CONSUMER - PERSONS WHO RETURN THIS [insert name of applicable device] MAY BE CONTACTED BY A SALESPERSON FOR THE PURPOSE OF SELLING [insert name of applicable product].

C. Failing to disclose clearly and conspicuously, at the beginning of any telephone call to any prospective customer, the fact that the individual making the call is either soliciting the sale, rental or lease of publications, merchandise or services for respondents, or is arranging for a sales solicitation to be made, and that if the prospective customer so agrees, the respondent concerned will send a salesperson to visit said prospect for the purpose of soliciting the sale, rental or lease of said publications, merchandise or services.

D. Visiting the home or place of business of any person for the purpose of soliciting the sale, rental or lease of any publications, merchandise or service, unless at the time admission is sought into the home or place of business of such person, a card 3 inches by 5 inches in dimension, with all words in 10-point boldface type, with the [184] following information, and none other, in the indicated order, is presented to such person:

(1) the name of the corporation;

(2) the name of the salesperson;

(3) the term "Encyclopedia Sales Representative" [or other applicable product];

(4) the terminology: "The purpose of this representative's call is to solicit the sale of encyclopedias" [or other applicable product].

E. Failing to present the card, required by Paragraph II D, above, to each such person, to direct each such person to read the information contained on such card, and to provide each such person with an adequate opportunity to read the card before engaging any such person in any sales solicitation.

F. Using the words "Mothers Club" or words of similar import and meaning to represent, directly or by implication, the existence of a *bona fide* educational program, club, or business entity which provides educational services or benefits to consumers or using any trade name misrepresenting in any manner the nature or purpose of their business. [185]

G. Representing, directly or by implication, either orally or in writing that:

(1) Any person calling on any prospective purchaser is:

(a) engaged in or connected with "advertising," "marketing," "promotion," "education," or anything other than the sale of encyclopedias or other educational or reference materials;

(b) conducting, taking or participating in a survey, opinion poll, interview or any other information gathering activity; or

(c) calling on said prospect for the primary purpose of delivering or disseminating any vacation gift certificate, prize, gift, gift certificate, chance in any contest, or any other merchandise or item or chance;

(2) only a few minutes will be required to complete the visit inside the prospective purchaser's home or place of business; or misrepresenting, [186] in any manner, the period of time required to complete the sales or other presentation;

(3) any person contacted has been specially selected to receive any offer; or misrepresenting, in any manner, the persons or class of persons to whom said offer is available;

(4) any encyclopedia or other reference material is a new publication, or a publication which has not been previously available to the public unless such is the fact, or misrepresenting, in any manner, the extent of editorial revisions, in any encyclopedia or other reference material;

(5) any offer is limited, must be accepted immediately or within a specified time period, or is a special offer, unless such is a fact; or misrepresenting, in any manner, the nature, scope or duration of any sales offer;

(6) any publication, merchandise or service is being offered free, without cost, as a bonus, reduced in price or otherwise to any prospective purchaser of any of respondents' publications, merchandise or services [187] agreeing to perform any advertising, promotional or selling function, including but not limited to, any of the following acts or similar acts:

(a) permitting their names to be listed as local owners of the product or services;

(b) providing the name of any person who may be interested in purchasing any publication, merchandise or service;

(c) writing a letter evaluating the merits of any publication or other item which may be used in advertising;

(d) displaying any publication or other item in a conspicuous location in his home;

(e) keeping any publication or other item current by purchasing an annual yearbook or by purchasing any research service;

(f) completing installment payments for any item in a period of time less than the period of time initially represented; or

(g) paying a membership fee in order to participate in the Consumer Buying Educational Service, or any other program, club, [188] service or entity which provides an opportunity for participants to purchase merchandise at a savings from the retail prices for such merchandise, or paying a fee to participate in any similar program, club, service or entity; or

(h) misrepresenting, in any manner, that any publication, merchandise or service is being offered free, without cost, as a bonus, or reduced in price to any person;

(7) any publication, merchandise or service is being offered free, without cost, or is given as a bonus or otherwise to any purchaser of any of respondents' publications, merchandise or services, pursuant to any agreement to purchase, rent or lease any other publication, merchandise, or service, or combination thereof, from such respondent, unless:

(a) the contract price for the purchase, rental or lease of any such other publication, merchandise, service, or combination thereof, has remained at the said price or above for at least six (6) months within the last [189] twelve (12) months immediately preceding the time at which the representation is made;

(b) no publication, merchandise or service has been offered free, without cost or given as a bonus or otherwise with the sale, rental or lease of any such other publication, merchandise, service or combination thereof, to any person for a period of at least six (6) months within the last twelve (12) months immediately preceding the time at which the representation is made;

(c) no publication, merchandise, service, or combination thereof, of equivalent or greater value, has been eliminated by such respondent from any such other publication, merchandise, service, or combination thereof, with which the free, without cost or bonus publication, merchandise or service is being offered; [190]

Provided, however, any such prices as are restricted by Paragraph II G (7)(a) of this order may be altered at any time by the respondent concerned to reflect *bona fide* changes in market conditions.

H. Misrepresenting, in any manner, the terms, conditions, method, rate or time of payment actually made available to any person.

I. Representing, directly or by implication, either orally or in writing that:

(a) any person using any research service will receive answers to questions on any subject; or misrepresenting, in any manner, the scope of, or restrictions imposed upon the use of, any such research service;

(b) any answer provided by a research service is the product of detailed, exhaustive or original research generated by the specific question asked by any person utilizing said service unless such is the fact; or misrepresenting, in any manner, the extent of individual attention, research, preparation or quality of any answer furnished by any such research service; [191]

(c) any answer provided by any research service is a suitable or acceptable substitute for any term paper, theme or other report; or misrepresenting, in any manner, the benefit or use of any answer provided by any research service;

(d) any research service is being offered at any price or that the research service has a retail value unless such is the fact;

(e) the cost to any respondent of any research service represents a retail value.

J. (1) Failing to disclose, clearly and conspicuously, in writing on all promotional materials describing any research service, and orally during the course of any sales or other presentation relating to said service, each condition or limitation placed upon the use of such research service.

(2) Failing to disclose applicable limitations on the time within which answers will be supplied by any research service in writing on all promotional materials and orally [192] during the course of any sales presentation relating thereto.

K. (1) Representing, directly or by implication, through the use of any oral statement, written quotation, picture or any other means that any publication, merchandise or service has received an endorsement, recommendation, or sponsorship from any educational, religious, or other institution or other entity or from any person, unless the stated endorsement is genuine and authentic in all respects, and discloses the year or edition of the publication to which such endorsements pertain, if a publication is involved.

(2) Using, publishing, or referring to any testimonial or endorsement unless (1) such use, publication, or reference is expressly authorized in writing and unless (2) respondents have good reason to believe that at the time of such use, publication, or reference, the person or organization named subscribes to the facts and opinions therein contained. [193]

(3) Representing, in any manner, that an endorsement or testimonial has been recently executed or is current unless this is the fact.

(4) Misrepresenting, in any manner, that any person is calling on a prospective customer with the endorsement, recommendation, or sponsorship of another person or organization.

L. Failing to disclose:

(1) clearly to the officials of any educational institution being visited, where a purpose of such visit is to obtain the institution's permission to disseminate through the institution promotional material which solicits the sale of any product to the parents of the children enrolled in the educational institution, and which is designed to secure leads for in-home sales presentations, prior to any such dissemination, that the purpose of disseminating such promotional materials is to secure leads for in-home sales presentations; [194]

(2) conspicuously on the face of such promotional materials within the scope of L(1) that dissemination of such promotional materials through the educational institution does not constitute an endorsement or a recommendation by the institution or its officials that such materials being promoted should be purchased unless such is the fact.

M. Representing to any person, directly or by implication, either orally or in writing that:

(1) any price is the retail, regular, usual or words of similar import or effect, price for any publication in any binding, merchandise or service, unless the respondent concerned is making a substantial number of its unit sales for each such publication in each such binding, merchandise or service, individually, at or above the represented price;

(2) any price is the retail, regular, usual, or words or similar import or effect, price for any set of publications in any binding and in combination with any other publication, [195] merchandise or service, unless the respondent concerned is making a substantial number of its unit sales for each such set of publications in each such binding individually or in combination at or above the represented price;

(3) savings may be realized by the purchase, rental or lease of any publication, merchandise or service, or any combination thereof, from any of respondents' former prices for its products unless:

(a) such savings claims are based upon retail, regular, or usual prices, or combination prices, arrived at in accordance with Paragraph II M(1) and (2) above;

(b) respondents clearly and conspicuously specify the publication, merchandise or service, or combination thereof, and the price from which the savings are to be realized; and

(c) the publication, merchandise or service is of comparable quality in all material respects with the publication, merchandise or service sold at the higher price; [196]

(4) savings may be realized by the purchase, rental or lease of any publication, merchandise or service, or any combination thereof, from comparable products of competitors unless:

(a) the respondent concerned clearly and conspicuously specifies the publication, merchandise or service, or combination thereof, from which the savings are to be realized;

(b) the price utilized for comparison purposes is the price at which a substantial number of persons have purchased the item referred to in (a) immediately above;

(c) the item referred to in (a) above is of comparable quality in all material respects to the product being sold; [197]

(d) respondents have in good faith conducted a market survey or obtained a similar representative sample of prices in the trade area where the comparison is made which establishes the validity of said compared price.

N. Misrepresenting in any manner, either orally or in writing:

(1) the amount of savings to be realized by any person who enters into an agreement with any respondent for any publication, merchandise or service; or

(2) that any publication, merchandise or service is being offered free or without charge, or is given to any such person.

O. Failing to comply with any and all provisions of the Commission's Trade Regulation Rule, *Cooling-Off Period For Door-To-Door Sales* (16 C.F.R. 429.1), which are in effect on the date this order becomes effective, and with any modifications or changes in the aforesaid Rule which may be made. A copy of the said Rule shall be made a part of this order for purposes of complying with other provisions hereof. [198]

P. Initiating contact with any purchaser through any means for any reason from the time said purchaser enters into any agreement containing a NOTICE OF CANCELLATION, as required by Paragraph II O of this order, until said buyer's cancellation period has expired.

Q. Failing to maintain a copy of each NOTICE OF CANCELLATION received pursuant to Paragraph II P of this order, and making said documents available for inspection and copying by the Commission's staff upon reasonable notice. Any respondent receiving such NOTICE shall maintain it for a period of three (3) years from date of receipt.

R. Failing to create adequate records, which shall be maintained for a period of three (3) years and made available to the Commission's staff for inspection and copying upon reasonable notice, from which the validity of any savings claims, retail price claims, comparative value claims, or other representations of the type described in Paragraphs II G(7), II M and II N of this order can be determined, and making any pricing claims within the scope of this provision unless there [199] are in existence for at least the six (6) months preceding such claims records from which the validity of such claims can be determined.

S. Failing to attach to any contract for the sale, rental or lease of any publication, merchandise, service or combination thereof a written statement that clearly and conspicuously discloses, and only discloses, the following information in the indicated order and manner:

(1) in 12-point boldface type size the terminology:

PRICE LIST

THE FOLLOWING PRICES ARE THE *ONLY* AUTHORIZED PRICES AT WHICH THE LISTED ITEMS MAY BE OFFERED. ANY PRICE NOT LISTED BELOW IS UNAUTHORIZED AND FALSE.

(2) a list of all publications, merchandise, services or combination thereof currently offered for sale, rental or lease, and in immediate conjunction thereto each price at which any respondent is authorized to offer said product or service pursuant to Paragraph II M of this order. [200]

(3) in 12-point boldface type the terminology, when applicable:

FREE ITEMS

ONLY THE FOLLOWING PRODUCTS AND SERVICES MAY BE OFFERED FREE. YOU ARE PAYING FOR ANY ITEMS RECEIVED AND NOT LISTED BELOW.

(4) a list of all publications, merchandise or services currently offered as free, without cost, or as a bonus pursuant to Paragraph II G(7) of this order.

T. Failing to orally instruct any person at the time said person signs any contract for sale, rental or lease, of any publication, merchandise, service or combination thereof, pursuant to an oral sales presentation, that a "Price List" is attached to said person's contract.

III

It is further ordered, That respondents Grolier, Incorporated, American Peoples Press, Inc., Americana Interstate Corp., Career Institute, Inc., Grolier Enterprises, Inc., and Grolier Reading Programs, Inc., corporations, and their successors or assigns, their officers, agents, representatives and employees, directly or indirectly, through any corporation, subsidiary or [201] division, or other device, in connection with the advertising, offering for sale, sale or distribution of any textbook, encyclopedia, reference or educational material, training course or teaching machine, or any other publication, merchandise or service through the use of any program, plan, method or device, that provides or purports to provide for the sale or distribution of any of said items to any person on an approval basis, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

A. Representing, directly or by implication, either orally or in writing that:

(1) any person has the option to receive each publication, merchandise or service, separately and individually, and to accept or reject same, unless such person is allowed in all instances to receive and to purchase or reject each such publication, merchandise or service separately and individually;

(2) any person will not receive any further publication, merchandise or service after the respondent concerned has received a timely notification of the person's cancellation of any such program, plan or method of sale [202] or distribution, unless such is the fact; or misrepresenting, in any manner, any consequence resulting from any person's cancellation of his participation in any such program, plan, or method of sale or distribution; and

(3) any person incurs no risk or obligation by joining or participating in any such program, plan, or method of sale or distribution; or misrepresenting, in any manner, any condition, right, duty or obligation imposed on any person.

B. Disseminating, or causing the dissemination of, any advertisement which fails to disclose in a clear and conspicuous manner:

(1) a description of the conditions and terms of any such program,

plan, or method of sale or distribution, and the duties, risks and obligations of any subscriber thereto; and

(2) a description of each publication, merchandise or service to be offered for sale, the billing charge to be made therefor, the anticipated total number of publications, merchandise or [203] services included in any such program, plan or method of sale or distribution, the number of publications, merchandise or services that will be included in each shipment of such items, and the number of and the intervals between each such shipment.

C. Failing to disclose, clearly and conspicuously, on any return coupon, order form or any other document used for responding to any such program, plan, or method of sale or distribution, the following information:

(1) the anticipated total number of publications, merchandise or services included in any such program, plan, or method of sale or distribution;

(2) the number of publications, merchandise or services that will be included in each shipment of such items; and

(3) the number of and the intervals between each such shipment.

D. Failing to disclose, clearly and conspicuously, in immediate conjunction with any publication, merchandise, service or notice thereof sent to any subscriber [204] the anticipated date on which the respondent from whom the subscriber obtained any of such items will initiate processing of the next shipment of any such item.

E. Failing to provide to any person in conjunction with each notice of any shipment of any publication, merchandise or service, a clear and conspicuous means by which said person may exercise his option or right to cancel said shipment, if such is his right.

IV

It is further ordered, That respondents Grolier, Incorporated, American Peoples Press, Inc., Americana Corporation, Americana Interstate Corp., Federated Credit Corp., Career Institute, Inc., Grolier Interstate, Inc., Grolier New Era Corp., Madison Enterprises, Inc., R. H. Hinkley Company, Spencer International Press, Inc., The Grolier Society, Inc., and The Richards Company, corporations, and their successors, assigns, officers, agents, representatives and employees, directly or indirectly, through any corporation, subsidiary, division or other device, in connection with the collection or attempted collection of any debt allegedly due and owing pursuant to any contract or other agreement relating to the purchase or other receipt of any textbook, encyclopedia, reference or educational material, [205] training course or teaching machine, or any other publication, merchandise or service, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

A. Representing, directly or by implication, either orally or in writing that:

(1) any company, corporation, or entity engaged in collection of monies allegedly due or owing to such concerns or any other company, corporation or entity has separate *bona fide* departments or divisions for legal matters, unless such are the facts; or misrepresenting, in any manner, the existence, or functions of any division or department of any company, corporation or entity;

(2) the Code of Federal Regulations, or any other federal regulation or statute, provides that any employee of the Federal Government who has any outstanding debt due or owing may be subject to dismissal from the federal service for failure to pay said debt unless the respondent concerned can demonstrate that sufficient facts exist with regard to the [206] employee to whom the representation was made which establish the propriety of such claim;

(3) any person who utilizes the United States mail to obtain any publication, merchandise or service and who fails to pay or becomes delinquent in paying for any such item will be subject to prosecution for mail fraud under federal law unless the respondent concerned can demonstrate that sufficient facts exist, with regard to person to whom the representation was made, which establish the propriety of such claim; or misrepresenting, in any manner, the rights, duties or obligations of any person arising from any federal, state, or local statute, ordinance, or regulation;

(4) any respondent utilizes the services of credit reporting companies or other entities or persons who disseminate credit information in a manner which will adversely affect the public or general credit rating of any person who has become delinquent in paying any debt unless the respondent concerned can demonstrate [207] that sufficient facts exist, with regard to the person to whom the representation was made, which establish the propriety of such claim; or misrepresenting, in any manner, that any person's public or general credit rating will be adversely affected;

(5) any letter, notice or other communication which has been prepared, originated or composed by any respondent has been prepared, originated or composed by any other person, firm or corporation;

(6) using any correspondence, forms or any written materials which appear to simulate or depict official legal process;

(7) suit will be instituted to recover any delinquent debt, or that any delinquent debt will be transferred to any attorney with instructions to institute suit, or that any other legal step to collect any outstanding debt will be taken, unless a definite date is set forth for such action and such are the facts; or misrepresenting, in any manner, respondents' relationship with, or instructions to, any attorney, or the course of action that will be taken by any attorney, [208] or misrepresenting in any manner that an account has been transferred to any person or entity for collection unless those are the facts.

V

For the purpose of the following provisions of this order, the term "respondents" shall apply to each of the respondents named in Paragraphs I and II of this order.

It is further ordered, That respondents:

A. Deliver, by registered mail, a copy of this order to each of their salesmen, agents, solicitors, independent contractors, or to any person engaged in the promotion, sale or distribution of any of the publications, merchandise or services included in this order, and to any person engaged by respondents to perform such duties in the future at the time such person is so engaged;

B. Obtain from each person described in Paragraph V A, a signed statement setting forth his intention to conform his business practices to the requirements of this order; retain said statement during the period of three (3) years thereafter; and make said statement available to the Commission's staff for inspection and copying upon reasonable notice; [209]

C. Advise each such present and future salesman, agent, solicitor, independent contractor or any person engaged in the promotion, sale or distribution of any of the publications, merchandise or services included in this order that respondents will terminate the engagement or services of any such person, unless such person agrees to and does furnish to respondents a statement required by Paragraph V B, above; and

D. If any such person will not agree to file a statement with respondents as required by Paragraph V B above, and be bound by the provisions of this order, the respondents shall immediately terminate the services of such person.

E. Furnish the Commission on a quarterly basis with a list of those independent or outside distributors whose retail installment contracts have been financed by respondents, their subsidiaries or affiliates.

VI

It is further ordered, That the respondents shall forthwith distribute a copy of this order to each of their operating divisions. [210]

VII

It is further ordered, That respondents shall notify the Commission at least thirty (30) days prior to any proposed change in any of the corporate respondents such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of which may affect compliance obligations arising out of this order.

VIII

It is further ordered, That respondents shall, within sixty (60) days after the effective date of this order, file with the Commission a report in writing setting forth in detail, the manner and form in which they have complied with this order.

APPENDIX A

NOTICE

Attached hereto are the *pertinent provisions* of a cease and desist order entered against Grolier, Incorporated and certain of its subsidiaries, including Grolier Interstate, Inc. by the Federal Trade Commission, an agency of the Federal Government. Violation of any provision of this order can result in severe monetary penalties to Grolier, Incorporated and Grolier Interstate, Inc. If you are employed by Grolier, Incorporated or any of its subsidiaries, you will be *required* to observe the provisions of this order. Violation of any provision of this order by an employee constitutes a violation of a federal law.

You should carefully read this order before agreeing to any employment arranged with Grolier, Incorporated or any of its subsidiary companies.

(President)
Grolier, Incorporated

OPINION OF THE COMMISSION

BY DOLE, *Commissioner:*

Grolier, Inc. and its wholly-owned subsidiaries,[1] [hereinafter referred to as "respondent"] appeal from the initial decision of

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[1] American Peoples Press, Inc., Americana Interstate Corp., Career Institute, Inc., Grolier Enterprises, Inc., Grolier Reading Programs, Inc., Americana Corporation, Spencer International Press, Inc., The Grolier Society, Inc., R. H. Hinkley Co., Grolier New Era Corp., The Richards Co., Inc., Madison Enterprises, Inc., Grolier Interstate, Inc., and Federated Credit Corp. were named as respondents and found by the Administrative Law Judge to be wholly-owned corporate subsidiaries of respondent Grolier, Inc. *See* I.D. Findings 2-15.

Administrative Law Judge Theodor P. von Brand that certain of respondent's practices violated Section 5 of the Federal Trade Commission Act. Complaint counsel have filed a cross-appeal.[2] [2]

Respondent is engaged in the publication and distribution of encyclopedias, other reference works and services, training courses, and teaching machines. Respondent sells its products door-to-door as well as through mail solicitations. Its products have included Encyclopedia Americana, Encyclopedia International, New Book of Knowledge, World's Greatest Classics, Book of Popular Science, and Children's Hour.[3] Both door-to-door selling and mail order solicitations account for substantial sales volume.[4]

On the basis of an extensive hearing record, the law judge sustained the complaint allegations that respondent has engaged in a host of deceptive and unfair practices. We agree with his determination that respondent has violated Section 5. Like the appeals before us, this opinion is directed mainly to the rather technical issues raised by the judge's proposed order to cease and desist.

The law judge's findings deal with respondent's personnel recruitment activities, sales and promotion practices, and debt collection procedures. With respect to personnel recruitment he found, *inter alia,* that respondent misrepresented that the jobs offered were non-selling positions and that the conditions placed upon salary or income guarantees were not disclosed to job applicants.[5] He also determined that respondent employed a variety of deceptive sales and promotional practices. For example, he concluded that respondent misrepresented the regular retail price of its products. [3] Furthermore the judge found that respondent had misrepresented to consumers the purpose of in-home sales presentations.[6]

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[2] For convenience, the following abbreviations are used in this opinion:

I.D. – Initial decision of the administrative law judge;
Tr. – Transcript of testimony;
Cx – Commission exhibit.

[3] Respondent has also sold products not published by Grolier, Inc. These include the Harvard Classics, The Bible, and the Hammond Atlas. *See* I.D. Finding 90.

[4] In 1969 respondent's door-to-door sales were $70,000,000 while mail order sales of certain subsidiaries accounted for $41.5 million. In 1970, sales door-to-door accounted for $63.4 million while mail order volume was $49 million. In 1972, mail order volume exceeded door-to-door sales by $63 million to $35.3 million, respectively. *See* I.D. Findings 16 and 17.

[5] *See* I.D. Findings 60-88.

[6] *See* I.D. Findings 114-132. In addition, the judge found that the salesmen of respondent Spencer International Press, Inc., in approaching parochial school principals, had misrepresented that they were from the "National Catholic Educator's Association" and that respondent Spencer's promotional packets, printed with a "bold cross in the upper left hand corner," as well as its follow-up phone talks and sales presentation had the capacity to lead parents to believe that the product had been endorsed by the parochial school or the archdiocese. *See* I.D. Finding 91-101. Respondent, The Richards Company, Inc., according to the law judge, distributed to its salesmen a picture of Pope Paul with the American People's Encyclopedia, although the Holy See had not endorsed the encyclopedia

(Continued)

The administrative law judge's order places respondent under a number of prohibitions and requires respondent to take certain affirmative actions. The order is directed to respondent's personnel recruiting practices, debt collection procedures, promotions aimed at schools to obtain entry to students' homes, misrepresentations as to the purpose of salesmen's calls and payment plans, misleading pricing claims and offers of free goods, and other unfair or deceptive advertising practices.

LIABILITY

While respondent addresses its appeal, in the main, to selected provisions of the judge's order, it also contends that the evidence adduced by complaint counsel at the hearing in this matter compels a dismissal of all counts of the complaint. *See* Respondents' Appeal Brief at 3. We find no merit in this argument or in respondent's alternative argument that complaint [4] counsel's evidence of Section 5 violations was *de minimis*. We have carefully reviewed the record in light of the initial decision and have found ample evidence to support the judge's findings. Respondent also contends that the evidence is insufficient to hold it accountable for any deceptive recruitment, sales or debt collection practices of its employees. We reject this contention. It is well settled that firms cannot avoid the requirements of Section 5 by passing off responsibility for deception to their employees. As the court stated in *Parke, Austin & Lipscomb, Inc.* v. *FTC*, 142 F.2d 437, 440 (2d Cir. 1944), "[H]owever unauthorized the offending conduct of the salesmen may have been and however condemned and discouraged by their superiors, it still was conduct which subjects the employers to the jurisdiction of the Commission and its cease and desist order." *See Goodman* v. *FTC*, 244 F.2d 584 (9th Cir. 1967). In any case, the record indicates that respondent initiated several of the illegal practices. We, therefore, adopt the judge's findings and conclusions, except to the extent they are inconsistent with the findings and conclusions set forth in this opinion.

ORDER PROVISIONS

I. Deceptive Recruitment Practices

The judge's order requires respondent in recruitment advertise-

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for commercial purposes. *See* I.D. Finding 184. Judge von Brand also determined that a letter written in 1953 by the President of the University of Notre Dame concerning a 1953 encyclopedia edition was used by respondent Spencer as promotional material, after the date had been removed, as late as 1969-70. *See* I.D. Finding 185.

ments to disclose that prospects will be hired to sell encyclopedias on an "in-home" basis.[7] The provision is based on the judge's finding that respondent recruited its door-to-door encyclopedia salesmen by affirmatively misrepresenting that the positions offered were in public relations work, marketing and promotions, sales administration and management.[8] Although phone numbers were listed in respondent's [5] recruitment advertisements, it was respondent's policy not to disclose over the phone the nature of the employment offered.[9] While some applicants were informed during their initial interview that the position involved encyclopedia sales,[10] other recruits did not realize that until training was actually in progress or had been completed.[11] In some instances recruits were explicitly told that the jobs did not involve selling.[12] Under these circumstances, the order provision requiring respondent to disclose in advertising that it is recruiting "encyclopedia salesmen" is necessary to prevent a continuation of the type of deception which has misled job applicants in the past.[13]

Respondent asserts that a simple "help wanted" ad would be in violation of the order,[14] and that an ad that includes no more than a telephone number does not mislead.[15] Respondent contends that an affirmative disclosure that the sole job responsibility is to solicit and sell encyclopedias in the home will effectively preclude recruitment advertisements.[16] However, in view of the affirmative misrepresentations as to the nature of the job which have been made both in advertising and at the initial interview, we conclude that the affirmative disclosure required by the order is justified. [6]

The law judge required[17] that certain paragraphs of the order[18] be furnished to applicants at the initial face-to-face interview. Respondent argues that it should be permitted, instead, to furnish the applicant with a summary of the order. The order does not preclude respondent from furnishing a prospective employee with an accurate explanation of the order, orally or in writing. The Commission has determined, however, not to modify the requirement that respondent furnish copies of the pertinent provisions specified. *See Encyclopedia Britannica, Inc.*[19]

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[7] Respondent argues that the evidence establishes only unauthorized and infrequent recruiting violations and that therefore no order provisions relating to recruitment should be included in the order. The administrative law judge, however, correctly found that respondent's recruitment advertisements frequently and affirmatively misrepresented that the positions offered were non-selling in nature, *see* I.D. Finding 60; that "management trainee" recruits were in fact hired to work as door-to-door salesmen, *see* I.D. Finding 67; and that respondent frequently advertised compensation guarantees for the positions offered without disclosing the conditions which applicants would be required to meet in order to receive the guaranteed compensation, *see* I.D. Findings 68 and 70.

[8] *See* I.D. Finding 60.

[9] *See* I.D. Finding 63.

[10] *See* I.D. Finding 73.

[11] *See* I.D. Finding 75.

[12] *See* I.D. Finding 76.

[13] *See* Order Paragraph I (C).

[14] *See* Respondents' Appeal Brief at 52.

[15] *See* Transcript of Oral Argument at 14 (remarks of Mr. Furth).

[16] *See* Transcript of Oral Argument at 14 (remarks of Mr. Furth). We note, however, that respondent's President and Chairman of the Board, Mr. Murphy, testified at the hearing that he would be amenable to a statement in recruitment advertising that the job involved direct selling in the home, *see* Tr. at 16458, and that on occasion he would be willing to disclose in advertising that the products to be sold were encyclopedias. *See* Tr. at 16459.

[17] Order Paragraph I (E).

[18] Paragraphs I, II and V.

II. Deceptive Sales and Promotion Practices

Respondent objects to the judge's order requirement that its sales representatives present a three inch by five inch card at the time admission is sought into the home for the purpose of soliciting sales. Respondent's representatives must direct the consumer to read the information contained on the card. The card discloses the name of the corporation, the name of the sales person, and the term "ENCYCLOPEDIA SALES REPRESENTATIVE" (or reference to other applicable product).

The record shows that respondent's sales representatives failed to disclose and have misrepresented the purpose of the in-home visit in both telephone calls to consumers and in door-to-door canvassing.[20] As Judge von Brand concluded:

> The purpose of respondents' sales representatives' contact, which is to sell, is a material fact in a prospect's decision to let such representative into [his] home. The failure to disclose at the [7] outset, and in many instances, to affirmatively misrepresent, the purpose of contacting prospective customers was false, misleading and deceptive.[21]

Respondent's assertion that instances of deception-at-the-door "are clearly isolated and untypical examples of individual sales representatives acting in contravention of respondents' corporate policies"[22] is contradicted by the record.[23] Both the sales manual issued under the letterhead of The Grolier Society, Inc. Publishers[24] and distributed to the company sales representatives,[25] as well as respondent Spencer's manual, instruct salesmen to affirmatively misrepresent the purpose of the in-home visit.[26]

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[19] 87 F.T.C. 421, 528 (1976), *appeal pending.* No. 76-1477 (7th Cir.).

[20] *See* I.D. Finding 108-130.

[21] I.D. Finding 132 (citation omitted). A similar requirement was included in the Commission's order in *Encyclopaedia Britannica, supra* 87 F.T.C. at 524, 527.

[22] Respondents' Appeal Brief at 56.

[23] *See* CX 419, Tr. at 664, 693-95 (testimony of Mr. Romano); CX 651A-C, Tr. at 5662-63; I.D. Finding 136.

[24] CX 563(a).

[25] *See* Tr. at 2836-38 and CX 563(a).

[26] "Hello, Mr./Mrs. blank, blank, blank? My name is blank, blank, blank, and I'm with the Grolier Society. I don't know whether that name means anything to you but Grolier is the world's largest publisher of educational reference books. We actually publish 20 different sets of Encyclopedias-but please do not be alarmed Mr./Mrs. blank, blank, blank, because *I didn't call you to give you a sales talk!* The purpose of my call is this:

(Continued)

[8] It is clear from the in-home presentation talks set forth in the manuals that the purpose of the in-home visit is to sell [9] the company's products.[27] Indeed, the instruction accompanying one of the telephone talks points out that "when you have an appointment you take your samples with you."[28]

Respondent has argued that the Commission should not mandate the exact disclosures to be made. Each of the disclosures required to be included on the card however is necessary to prevent future violations. While respondent might be allowed to make undefined, "appropriate" disclosures, such an order provision would inject unnecessary uncertainty into respondent's compliance obligations.

Respondent also suggests as an alternative to the 3x5 card the use of a normal size business card. However, if all of the necessary information were included on a business card, the print would be so small that the disclosure would be unintelligible. Moreover, business cards are normally accepted for purposes of future reference, whereas the purpose of this requirement is to encourage the consumer immediately to refer to the card so that he will be placed

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"Grolier has approximately 7,000 sales people across the country and we have to provide these sales people with prospects to call on. Right now we are getting some help from several families in each community and in return for that help we are paying these families in Grolier merchandise. . . .

"Notes: If prospect says they won't be home then set it up for tomorrow night–or for Sat. and Sun.

"If prospect says they are not interested–say 'That's fine–all I want to do is explain what we are doing and like I said I am not coming out there to give you a sales talk.' "

CX 563(i) (emphasis in original)

Telephone talk number II makes the same affirmative misrepresentation. *See* CX 563(o).

Respondent Spencer International Press, Inc. likewise utilized a training manual which contained both a "door approach" and "telephone talk" that misrepresented the purpose of the in-home visit. *See* CX 871-F; CX 871-V; I.D. Finding 100. The training manual instructed the sales representative to:

FOLLOW PRESENTATION - *Do not deviate* - it must be done our way, which is the successful way. CX 871-B (emphasis in original). The door approach set forth in the training manual is as follows:

Hi, I wonder if you could give me some information? (wait for reaction)

I'm conducting a series of special interviews in the ________ area this evening and I was supposed to ask you and the Mrs. a couple of questions. (show questionnaire) By the way my name is ________. (Hold out hand) Do you mind if I step in? (If ques. use follow up. Also when known, use family name)

CX 871-F.

The Telephone Talk represents the home visitor as an "instructor" in programmed learning:

Hello. Is this Mrs. ________ ? Good! This is Mr. ________ calling from the Catholic School Division of Programmed Learning. I'm calling in reference to the announcements the children took home from *(Name)* School. (Pause.) You probably remember it. As you know, we agreed to give each family a free demonstration on programmed learning as a public service. And the reason I'm calling now is that our instructors will be in the *(Name)* area tonight. I thought I'd call first to make sure both you and Mr. ________ will be in this evening. It takes around 10 minutes, since each instructor sees about 6 or 7 families an evening. . . .

CX 871-V.

Judge von Brand found that certain of respondent's documents contain directives that full disclosure be made of the identity of the callers and the purpose of the call. He found further that these documents reflected the company's "official policy." *See* Finding 126. We disagree. This label is inconsistent with the evidence in the record and with other findings of the administrative law judge. *See, e.g.*, Finding 129. Accordingly we have modified Finding 126 by deleting the statement that "respondents' official policy prohibited misrepresenting to a prospective customer the purpose of a telephone call or home visit."

[27] *See* CX 563 J-K; CX 871 P-T.

[28] CX 563-1 and O.

"You have now prepared your prospects for the next step which is the presentation of products. *Do not* ask them if you can go get your samples. *Do it!!*" CX 563-k.

on notice that the caller is there for the purpose of selling him a set of encyclopedias.

We are not persuaded by respondent's argument that the "notice to consumer" provisions of the order are unjustified. This portion of the order requires that lead-gathering advertising which, for example, invites participation in a contest, contain a disclosure that consumers who respond may be contacted by a salesperson for the purpose of selling the applicable products. As the judge concluded, respondent's lead-generating advertising failed to disclose this material fact.[29] Furthermore, certain of the advertising in question creates the [10] impression that the consumer who responds to an offer of free information will receive delivery by mail and will not be subjected to a salesman's call.[30]

With respect to the proposed disclosure in the lead-getting material respondent objects to the requirement that it be placed in ten point boldface type and also renews its argument that the Commission should not prescribe specific language.[31] We find that it is necessary to place this important language in ten point boldface to assure that the consumer will be apprised of the message. The proposed language includes a disclosure that the consumer may be contacted by a sales representative for the purpose of selling the applicable product. There is no question that the main purpose of respondent's sales representatives in contacting persons at their homes is to sell its products. Any other assertion or inference would be deceptive. [11]

We turn now to respondent's objections concerning the pricing provisions of the order.[32] Respondent's contract, adjoining the retail price list, states that "a combination purchase of two or more of the products shown in bold face automatically entitles the customer to an approximate 30% price advantage from the individual prices. If, however, you purchase just one product you pay the full price shown."[33] The prices listed for the designated publications, however, are not the prices at which significant numbers of sales are made.[34] They represent the prices charged when the products are sold on an individual basis and sales of individual publications constitute only a small percentage of respondent's sales.[35] The law judge found that the sales representatives are frequently not even authorized to make individual sales of the publication or are discouraged from doing so. Respondent's sales representatives are trained instead to sell the products in combination, and respondent distributes standard combination schedules to its respective sales representatives which set forth the various publications included in each combination as well as the price of each combination.[36] We take the title "retail price list" to be tantamount to a representation that these are regular prices at which the designated publications have been sold. In view of the fact that the publications were only rarely sold at these prices, the list deceptively represented to consumers that cost savings could be realized through combination purchases.[37]

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[29] *See* I.D. Finding 105, I.D. p. 149.

[30] The copy at the end of respondent's "Uncle George" ad, CX 1614-H, states:

> Now we've run out of space, but we would like to tell you more. So please send for our free brochure. The coupon below will bring it . . . .

The coupon which the consumer is requested to send in states in part:

> Gentlemen:
>
> I am interested and would like to know more. I understand there's no charge and no obligation. . . .

Ibid. See CX 1614-G.

[31] Order Paragraph II (A) requires the following disclosure in lead-gathering advertising.

> *NOTICE TO CONSUMER* - PERSONS WHO REPLY AS REQUESTED MAY BE CONTACTED BY A SALESPERSON FOR THE PURPOSE OF SELLING [insert name of applicable product].

Order Paragraph II (B) requires a similar disclosure on the coupon used to respond to the advertisement.

> *NOTICE TO CONSUMER* - PERSONS WHO RETURN THIS [insert name of applicable device] MAY BE CONTACTED BY A SALESPERSON FOR THE PURPOSE OF SELLING [insert name of applicable product].

[32] Order Paragraphs II (M) and (S).

[12] The order recommended by the judge, therefore, prohibits respondent from representing a price for a product as its regular retail price unless substantial sales are made at the level represented as the regular price. In addition, the order requires that respondent attach to each contract a list of all products and services and, in immediate conjunction thereto, the actual selling price

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[33] I.D. Finding 158.

[34] I.D. Findings 158 and 160.

[35] I.D. Finding 157. *See* I.D. Finding 89.

[36] *See* I.D. Findings 89, 157-58. Indeed, beginning in late 1973 respondent added a statement to the retail price list which disclosed that "only a small fraction of Grolier's sales of any of these products is on an individual basis." I.D. Finding 158.

[37] We uphold the order provisions which address respondent's "continuity programs" and other methods of selling its products by mail on an approval basis. Under the "continuity programs" respondent would ship the first three volumes of a set singly, at intervals, but transmitted the balance of the set in one shipment unless the customer had tendered a timely notice of cancellation. The judge found that respondent failed to disclose that a bulk shipment of the remaining volumes would be made after shipment of the first three volumes. *See* I.D. Finding 230 and I.D. p. 166. Respondent argues that these order provisions are unwarranted since, prior to the issuance of the Part III complaint in this matter, it followed a policy of "full disclosure" of shipment sequences. However, the Commission has been "parsimonious, if not totally unyielding, in its adjudicative recognition of the defense of abandonment, and courts have been reluctant to vacate Commission orders on those grounds except in the most extreme circumstances not present here, such as where a corporate respondent had exited from the relevant lines of business under circumstances in which reentry seemed improbable." *See Fedders Corp.*, 85 F.T.C. 38, 72 (1975), *aff'd*, 529 F.2d 1398 (2d Cir.), *cert. denied*, 429 U.S. 818 (1976).

In addition, respondent contends that the testimony of customers called by complaint counsel was not sufficient to support this portion of the order. Respondent's arguments are untenable. Moreover, as the administrative law judge observed:

> Respondents have also represented that persons joining or participating in such programs do so at no risk or obligation. However, participating in such continuity programs did entail certain risks and obligations. Consumers were subject to the risk of receiving a bulk shipment if the negative option provided by respondents was not successfully exercised. If books were not wanted, the consumer had to reject them and do so within the allotted time. If a timely notice of cancellation was not received due to delays in the mail, they risked being billed for publications even after such publications had been returned. I.D. p. 166.

pursuant to the "substantial" sales standard. The price list will enable the contracting consumer to judge whether the offer is a bargain—to compare [13] the contract with the authorized list prices and determine whether or not any savings claims are true. *Encyclopaedia Britannica, supra.*[38]

Complaint counsel advocate the adoption of an order provision which would prohibit respondent from representing that a price is a regular retail price unless, for the previous 6 month period, at least 30 percent of its sales for that product have been made at the price, or a higher price. As in *Encyclopaedia Britannica*[39] we are not persuaded that the order should depart from the Commission's guides on deceptive pricing, 16 C.F.R. 233, which provide, *inter alia*, that the retail price may be described as a selling price if "substantial" sales are made at the retail level.

Both respondent and complaint counsel object to Paragraph V of the proposed order. In essence Paragraph V requires respondent to furnish each person engaged in the promotion, distribution and sale of respondent's products and services, including independent contractors (distributors), with a copy of the order; to obtain a signed statement from each person declaring his intention to conform his business practices with the requirements of the order; and to cease doing business with each person who will not so sign. Respondent points to certain findings in the initial decision that respondent neither controlled nor was responsible for the actions of distributors.[40] For example, when respondent, The Richards Company, withdrew from direct sales, most of the company's key sales personnel became distributors.[41] While [14] respondent furnished assistance to the former Richards employees in helping them become distributors,[42] the law judge concluded that

> [b]y and large, . . . the contacts between respondent's officials and these distributors are not inconsistent with a finding that they were normal business communications such as may be expected of any manufacturer and his outside retailers. On balance, the evidence does not sustain a finding that respondents controlled or are responsible for the actions of such distributors.[43]

Complaint counsel, while conceding that Paragraph V should not apply to wholly independent distributors whose only connection with respondent is the purchase of books for resale to consumers, contend, nevertheless, that independent distributors who maintain a significant connection[44] with respondent should be subject to this order provision. Complaint counsel argue that there is a "very real possibility that the respondents will attempt to do, through distributors, what the Order prohibits them from doing directly."[45] We are not persuaded that it is necessary to include independent contractors within the purview of Paragraph V, and we have modified the order accordingly.[46] Should the violations addressed in these [15] proceedings be practiced by persons other than respondent's salesmen or agents, the Federal Trade Commission Act[47] affords sufficient means of proceeding against the alleged offenders.[48]

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[38] 87 F.T.C. at 529.

[39] *Id.*

[40] *See* I.D. Findings 276-288 and I.D. p. 172.

[41] I.D. Finding 282.

[42] *See* I.D. Findings 283-86.

[43] I.D. p. 172.

Procedural Issues

As the final matter, we now consider respondent's procedural arguments. Respondent reasserts in its appeal a claim which the Commission has dealt with previously in this proceeding, that Judge von Brand should have been disqualified from conducting the hearing. The Commission concluded in its prior order addressing this issue[49] that Judge von Brand would not be subject to disqualification even if it could be shown that, while serving as attorney advisor to Commissioner MacIntyre, he advised the former Commissioner on matters pertaining to respondent. Respondent has marshalled no additional arguments in its briefs which dissuade us from this view.[50] Respondent asserts that "an attorney advisor bears an ethical responsibility as stringent as that of the [16] Commissioners themselves"[51] and therefore that Judge von Brand should be disqualified. The fallacy in respondent's argument is that the

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[44] Complaint counsel would apply Paragraph V to persons or entities: (1) receiving direction, control or approval from respondent for sales practices; (2) receiving promotional materials or sales aids from respondent; or (3) receiving financing from respondent for any contracts procured.

[45] Answering Brief of Counsel Supporting the Complaint at 54.

[46] *Compare National Housewares, Inc.*, Dkt. 8733, Opinion and Final Order (November 19, 1977). There, respondent Emdeko developed and refined an illegal "package selling scheme" and actively promoted its adoption by distributors. Unlike *National Housewares*, respondent cannot be said to be "active participants in the illegal practices," *id.* at 18–19 (slip opinion), of the distributors. Now would its conduct subject it to liability "closely akin to the liability of a contributing 'tort feasor,' " *id.* at 13 (slip opinion).

[47] 15 U.S.C. 45(m)(1)(B).

We also note that other portions of the order place restrictions upon possible attempts by the respondent to accomplish, through distributors, what the order prohibits it from doing directly. *See* Order Paragraph 1(F).

[48] The judge's order requires that respondent furnish the Commission with the names of the independent distributors with whom it does business and we adopt this provision. In addition, we will require respondent to furnish the addresses of its independent distributors and have modified Paragraph V accordingly.

[49] 87 F.T.C. 179 (1976).

[50] In conjunction with respondent's arguments as to disqualification of the law judge, respondent contends that the Commission was in error in denying discovery of certain documents reasonably calculated to lead to evidence concerning contacts between the Commissioners and the respondent during the period in which Judge von Brand was an attorney advisor. We reaffirm our ruling. 87 F.T.C. at 180–81.

[51] Transcript of Oral Argument at 6 (remarks of Mr. Furth.)

Federal Trade Commission Act provides for participation by Commissioners in both the investigative and the adjudicative stages of a proceeding.[52] Section 554(d) of the Administrative Procedure Act explicitly recognizes the dual role of "members of the body comprising the agency;" that legislation specifically authorizes a member's participation in both the investigative-prosecutorial function and the adjudicative decision-making process.

Respondent also appeals the denial of its motion to dismiss or stay the adjudicative proceedings and contends that the Commission should proceed by way of an industrywide trade regulation rule. It argues that while a principal competitor[53] is subject to similar affirmative relief provisions, other competitors are not.

While rulemaking would not necessarily be inappropriate in this circumstance, it is well established that the Commission may proceed by adjudication against an alleged offender without simultaneously pursuing all others. *Moog Industries* v. *FTC*, 355 U.S. 411, 413 (1958). The Commission, of course, does not have "unbridled power to institute proceedings which will arbitrarily destroy one of many law violators in an industry." *FTC* v. *Universal-Rundle Corp.*, 387 U.S. 244, 251 (1967). However, respondent has not substantiated its claim that the order provisions would cause substantial economic injury to its business. The record in this case demonstrates egregious violations of the Federal Trade Commission Act and the order imposed by the Commission is reasonably related to the violation and necessary to correct these abuses.[54]

[17] Having considered the arguments of respondent and com-

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[52] *See* 15 U.S.C. 45(b) and 49.

[53] *Encyclopaedia Britannica, supra.*

[54] Respondent's claim of "fundamental unfairness" as to the card-at-the-door and the advertising and promotional disclosure provisions is without merit.

We also reject respondent's contention that it was error for the administrative law judge to deny respondent's request to call as a witness a former director of the Commission's Office of Policy Planning and Evaluation. Respondent sought his testimony with respect to whether or not alternative relief provisions might be incorporated in the order which were "less drastic" than those proposed by the law judge. We cannot find that the judge abused his discretion in denying this request.

We uphold the administrative law judge's determination to deny discovery of an internal staff memorandum, entitled "Analytical Program Guide for the Direct Selling Industry," and related documents. Respondent sought the memorandum to support its assertion that the Commission has prejudged this proceeding, upon the basis of "secret evidence and secret law." Respondent's Appeal Brief at 38. The Commission's determination and its order in this matter rest solely upon the record compiled in Dkt. 8879. *See Encyclopaedia Britannica, Inc.*, 87 F.T.C. 378 (1976).

Also without merit is respondent's argument that it was error to deny it access to the total number of complaints and the subject matter of each complaint received from its customers by the Federal Trade Commission. The complaint information is relevant, according to respondent, to the formulation of appropriate relief. Specifically, respondent would seek to show "if negligible consumer injury or dissatisfaction has resulted from the practice which the particular form of relief is designed to rectify." Respondents' Appeal Brief at 39. The administrative law judge noted that the presence or absence of consumer complaints is of marginal utility in the formulation of the order provisions. Moreover, as stated by the law judge in denying discovery of the complaint information, the request was made "at a late stage of the proceeding. . .in the midst of trial." His denial of respondent's request for complaint information cannot be said to constitute an abuse of discretion.

plaint counsel in this matter, we have determined that the public interest is best served by the issuance of the appended order.

FINAL ORDER

This matter having been heard by the Commission upon the cross-appeals of complaint counsel and respondents' counsel from the initial decision and upon briefs and oral argument in support thereof and opposition thereto, and the Commission, for the reasons stated in the accompanying Opinion, having determined to sustain the initial decision with certain modifications:

It is ordered, That pages 1-176 of the initial decision of the administrative law judge be, and they hereby are, adopted as the Findings of Fact and Conclusions of Law of the Commission, except to the extent modified or otherwise indicated in the accompanying Opinion and except for the following: delete in Finding 126 the first sentence and the words "In fact" in the second sentence.

Other Findings of Fact and Conclusions of Law of the Commission are contained in the accompanying Opinion.

It is further ordered, That the following order to cease and desist be, and it hereby is, entered: [2]

ORDER

I

It is ordered, That respondents Grolier, Incorporated, Americana Corporation, Grolier Interstate, Inc., Grolier New Era Corp., Madison Enterprises, Inc., R. H. Hinkley Company, The Grolier Society, Inc., Spencer International Press, Inc. and The Richards Company, Inc., corporations, and their successors, assigns, officers, agents, representatives and employees, directly or indirectly, through any corporation, subsidiary, division or other device, in connection with the recruitment, training, or orientation of any person to sell, rent, lease, or distribute any textbook, encyclopedia, reference or educational material, training course or teaching machine, or any other publication, merchandise or service, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

A. Representing, directly or by implication, either orally or in writing, that:

(1) any respondent is offering positions in such fields as advertising, education, public relations, marketing, interviewing, or in any field other than door-to-door [3] sales, if door-to-door sales is included, to any extent, in the position for which persons are being

recruited; or misrepresenting, in any manner, the job for which any person is being solicited;

(2) persons will be trained as management trainees, or for other positions of responsibility concerned with administrative office functions, unless, in fact, a formal management training program is available to persons accepting employment on the basis of such representations; or misrepresenting, in any manner, the amount and type of training that will be given;

(3) any person who may be employed will contact prospects in their homes or places of business for the purposes of conducting surveys, advertising promotions, educational instruction or other nonselling functions; or misrepresenting, in any manner, the purposes for which any person is engaged. [4]

B. Misrepresenting, in any manner, the amount of income to be earned by any person or that may be earned by any person, the method of payment, or any condition or limitation imposed upon the compensation of any person, or the degree of ease or difficulty in performing any said condition imposed.

C. Failing to disclose, clearly and conspicuously, in all advertising offering employment in any way involving door-to-door sales:

(1) that the respondent concerned is recruiting persons for the sole purpose of soliciting or selling;

(2) that such soliciting or selling will be on an "in home" basis;

(3) that the products or services being sold are encyclopedias or services to be used in connection therewith, or in the event that encyclopedias or such related services are not being sold, the products and services being sold; and

(4) the basis for compensating persons so engaged. [5]

D. Failing to clearly and conspicuously advise, both orally and in writing, any prospective salesperson at the initial face-to-face interview, and prior to executing any employment agreement with any such person, the following information:

(1) all those disclosures set forth in Paragraph I C above;

(2) a complete and detailed description of each condition and limitation imposed upon the receipt of any compensation;

(3) where applicable, notification that such person will not be paid for time spent during orientation and training;

(4) a complete and detailed description of any expense or expenses any such person may incur in performing the required duties; and

(5) the percentage of persons holding similar positions engaged by the office offering the position during the twelve (12) months immediately preceding the offer, who have actually received an

equivalent, or greater, income than that promised under the terms of any such agreement. [6]

E. Failing to furnish to each applicant at the initial face-to-face interview and prior to executing any employment agreement with any such person, a copy of Paragraphs I, II and V of this order together with a cover letter as set forth in *Appendix A* attached hereto.

F. Making, distributing or using any training tapes, sales manuals, or any other document, method or device which contains any representation or instruction inconsistent with any provision of Paragraph I or Paragraph II of the order.

II

It is ordered, That respondents Grolier, Incorporated, Americana Corporation, Grolier Interstate, Inc., Grolier New Era Corp., Madison Enterprises, Inc., R. H. Hinkley Company, The Grolier Society, Inc., Spencer International Press, Inc., and The Richards Company, Inc., corporations and their successors, assigns, officers, agents, representatives, and employees, directly or indirectly, through any corporation, subsidiary, division or other device, in connection with the publishing, advertising, offering for sale, sale, rental, lease or distribution of any textbook, encyclopedia, reference or educational material, training course or teaching machine, [7] or any other publication, merchandise or service, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

A. Disseminating or causing to be disseminated, any advertisement or promotional material which solicits participation in any contest, drawing or sweepstakes, or solicits any response to any offer of merchandise, service or information unless any such solicitation clearly and conspicuously discloses the following statement in 10-point boldface type: NOTICE TO CONSUMER – PERSONS WHO REPLY AS REQUESTED MAY BE CONTACTED BY A SALESPERSON FOR THE PURPOSE OF SELLING [insert name of applicable product].

B. Providing any return card, coupon or other device which is used to respond to any advertisement or promotional material covered by Paragraph II A above, unless the following statement clearly and conspicuously appears in 10-point boldface type in immediate proximity to the space provided for a signature or other identification of the responding party: [8] NOTICE TO CONSUMER – PERSONS WHO RETURN THIS [insert name of applicable device] MAY BE CONTACTED BY A SALESPERSON FOR THE PURPOSE OF SELLING [insert name of applicable product].

C. Failing to disclose clearly and conspicuously, at the beginning of any telephone call to any prospective customer, the fact that the individual making the call is either soliciting the sale, rental or lease of publications, merchandise or services for respondents, or is arranging for a sales solicitation to be made, and that if the prospective customer so agrees, the respondent concerned will send a salesperson to visit said prospect for the purpose of soliciting the sale, rental or lease of said publications, merchandise or services.

D. Visiting the home or place of business of any person for the purpose of soliciting the sale, rental or lease of any publications, merchandise or service, unless at the time admission is sought into the home or place of business of such person, a card 3 inches by 5 inches in dimension, with all words in 10-point boldface type, with the [9] following information, and none other, in the indicated order, is presented to such person:

(1) the name of the corporation;

(2) the name of the salesperson;

(3) the term "Encyclopedia Sales Representatives" [or other applicable product];

(4) the terminology: "The purpose of this representative's call is to solicit the sale of encyclopedias" [or other applicable product].

E. Failing to present the card, required by Paragraph II D, above, to each such person, to direct each such person to read the information contained on such card, and to provide each such person with an adequate opportunity to read the card before engaging any such person in any sales solicitation.

F. Using the words "Mothers Club" or words of similar import and meaning to represent, directly or by implication, the existence of a *bona fide* educational program, club, or business entity which provides educational services or benefits to consumers or using any trade name misrepresenting in any manner the nature or purpose of their business. [10]

G. Representing, directly or by implication, either orally or in writing that:

(1) Any person calling on any prospective purchaser is:

(a) engaged in or connected with "advertising," "marketing," "promotion," "education," or anything other than the sale of encyclopedias or other educational or reference materials;

(b) conducting, taking or participating in a survey, opinion poll, interview or any other information gathering activity; or

(c) calling on said prospect for the primary purpose of delivering or disseminating any vacation gift certificate, prize, gift, gift certificate, chance in any contest, or any other merchandise or item of chance;

(2) Only a few minutes will be required to complete the visit inside the prospective purchaser's home or place of business; or misrepresenting, [11] in any manner, the period of time required to complete the sales or other presentation;

(3) any person contacted has been specially selected to receive any offer; or misrepresenting, in any manner, the persons or class of persons to whom said offer is available;

(4) any encyclopedia or other reference material is a new publication, or a publication which has not been previously available to the public unless such is the fact, or misrepresenting, in any manner, the extent of editorial revisions, in any encyclopedia or other reference material;

(5) any offer is limited, must be accepted immediately or within a specified time period, or is a special offer, unless such is a fact; or misrepresenting, in any manner, the nature, scope or duration of any sales offer;

(6) any publication, merchandise or service is being offered free, without cost, as a bonus, reduced in price or otherwise to any prospective purchaser of any of respondents' publications, merchandise or services [12] agreeing to perform any advertising promotional or selling function, including but not limited to, any of the following acts or similar acts:

(a) permitting their names to be listed as local owners of the product or services;

(b) providing the name of any person who may be interested in purchasing any publication, merchandise or service;

(c) writing a letter evaluating the merits of any publication or other item which may be used in advertising;

(d) displaying any publication or other item in a conspicuous location in his home;

(e) keeping any publication or other item current by purchasing an annual yearbook or by purchasing any research service;

(f) completing installment payments for any item in a period of time less than the period of time initially represented; or

(g) paying a membership fee in order to participate in the Consumer Buying Educational Service, or any other program, club, [13] service or entity which provides an opportunity for participants to purchase merchandise at a savings from the retail prices for such merchandise, or paying a fee to participate in any similar program, club, service or entity; or

(h) misrepresenting, in any manner, that any publication, merchandise or service is being offered free, without cost, as a bonus, or reduced in price to any person;

(7) any publication, merchandise or service is being offered free, without cost, or is given as a bonus or otherwise to any purchaser of any of respondents' publications, merchandise or services, pursuant to any agreement to purchase, rent or lease any other publication, merchandise, or service, or combination thereof, from such respondent, unless:

(a) the contract price for the purchase, rental or lease of any such other publication, merchandise, service, or combination thereof, has remained at the said price or above for at least six (6) months within the last [14] twelve (12) months immediately preceding the time at which the representation is made;

(b) no publication, merchandise or service has been offered free, without cost or given as a bonus or otherwise with the sale, rental or lease of any such other publication, merchandise, service or combination thereof, to any person for a period of at least six (6) months within the last twelve (12) months immediately preceding the time at which the representation is made;

(c) no publication, merchandise, service, or combination thereof, of equivalent or greater value, has been eliminated by such respondent from any such other publication, merchandise, service, or combination thereof, with which the free, without cost of bonus publication, merchandise or service is being offered; [15]

Provided, however, any such prices as are restricted by Paragraph II G (7) (a) of this Order may be altered at any time by the respondent concerned to reflect *bona fide* changes in market conditions.

H. Misrepresenting, in any manner, the terms, conditions, method, rate or time of payment actually made available to any person.

I. Representing, directly or by implication, either orally or in writing that:

(a) any person using any research service will receive answers to questions on any subject; or misrepresenting, in any manner, the scope of, or restrictions imposed upon the use of, any such research service;

(b) any answer provided by a research service is the product of detailed, exhaustive or original research generated by the specific question asked by any person utilizing said service unless such is the fact; or misrepresenting, in any manner, the extent of individual attention, research, preparation or quality of any answer furnished by any such research service; [16]

(c) any answer provided by any research service is a suitable or acceptable substitute for any term paper, theme or other report; or misrepresenting, in any manner, the benefit or use of any answer provided by any research service;

(d) any research service is being offered at any price or that the research service has a retail value unless such is the fact;

(e) the cost to any respondent of any research service represents a retail value.

J. (1) Failing to disclose, clearly and conspicuously, in writing on all promotional materials describing any research service, and orally during the course of any sales or other presentation relating to said service, each condition or limitation placed upon the use of such research service.

(2) Failing to disclose applicable limitations on the time within which answers will be supplied by any research service in writing on all promotional materials and orally [17] during the course of any sales presentations relating thereto.

K. (1) Representing, directly or by implication, through the use of any oral statement, written quotation, picture or any other means that any publication, merchandise or service has received an endorsement, recommendation, or sponsorship from any educational, religious, or other institution or other entity or from any person, unless the stated endorsement is genuine and authentic in all respects, and discloses the year or edition of the publication to which such endorsements pertain, if a publication is involved.

(2) Using, publishing, or referring to any testimonial or endorsement unless (1) such use, publication, or reference is expressly authorized in writing and unless (2) respondents have good reason to believe that at the time of such use, publication, or reference, the person or organization named subscribes to the facts and opinions therein contained. [18]

(3) Representing, in any manner, that an endorsement or testimonial has been recently executed or is current unless this is the fact.

(4) Misrepresenting, in any manner, that any person is calling on a prospective customer with the endorsement, recommendation, or sponsorship of another person or organization.

L. Failing to disclose:

(1) clearly to the officials of any educational institution being visited, where a purpose of such visit is to obtain the institution's permission to disseminate through the institution promotional material which solicits the sale of any product to the parents of the children enrolled in the educational institution, and which is designed to secure leads for in-home sales presentations, prior to any such dissemination, that the purpose of disseminating such promo-

tional materials is to secure leads for in-home sales presentations; [19]

(2) conspicuously on the face of such promotional materials within the scope of L(1) that dissemination of such promotional materials through the educational institution does not constitute an endorsement or a recommendation by the institution or its officials that such materials being promoted should be purchased unless such is the fact.

M. Representing to any person, directly or by implication, either orally or in writing that:

(1) any price is the retail, regular, usual or words of similar import or effect, price for any publication in any binding, merchandise or service, unless the respondent concerned is making a substantial number of its unit sales for each such publication in each such binding, merchandise or service, individually, at or above the represented price;

(2) any price is the retail, regular, usual, or words of similar import or effect, price for any set of publications in any binding and in combination with any other publication, [20] merchandise or service, unless the respondent concerned is making a substantial number of its unit sales for each such set of publications in each such binding individually or in combination at or above the represented price;

(3) savings may be realized by the purchase, rental or lease of any publication, merchandise or service, or any combination thereof, from any of respondents' former prices for its products unless:

(a) such savings claims are based upon retail, regular, or usual prices, or combination prices, arrived at in accordance with Paragraph II M(1) and (2) above;

(b) respondents clearly and conspicuously specify the publication, merchandise or service, or combination thereof, and the price from which the savings are to be realized; and

(c) the publication, merchandise or service is of comparable quality in all material respects with the publication, merchandise or service sold at the higher price; [21]

(4) savings may be realized by the purchase, rental or lease of any publication, merchandise or service, or any combination thereof, from comparable products of competitors unless:

(a) the respondent concerned clearly and conspicuously specifies the publication, merchandise or service, or combination thereof, from which the savings are to be realized;

(b) the price utilized for comparison purposes is the price at which a substantial number of persons have purchased the item referred to in (a) immediately above;

(c) the item referred to in (a) above is of comparable quality in all material respects to the product being sold; [22]

(d) respondents have in good faith conducted a market survey or obtained a similar representative sample of prices in the trade area where the comparison is made which establishes the validity of said compared price.

N. Misrepresenting in any manner, either orally or in writing:

(1) the amount of savings to be realized by any person who enters into an agreement with any respondent for any publication, merchandise or service; or

(2) that any publication, merchandise or service is being offered free or without charge, or is given to any such person.

O. Failing to comply with any and all provisions of the Commission's Trade Regulation Rule, *Cooling-Off Period For Door-To-Door Sales* (16 C.F.R. 429.1), which are in effect on the date this order becomes effective, and with any modifications or changes in the aforesaid Rule which may be made. A copy of the said Rule shall be made a part of this order for purposes of complying with other provisions hereof. [23]

P. Initiating contact with any purchaser through any means for any reason from the time said purchaser enters into any agreement containing a NOTICE OF CANCELLATION, as required by Paragraph II O of this order, until said buyer's cancellation period has expired.

Q. Failing to maintain a copy of each NOTICE OF CANCELLATION received pursuant to Paragraph II O of this order, and making said documents available for inspection and copying by the Commission's staff upon reasonable notice. Any respondent receiving such NOTICE shall maintain it for a period of three (3) years from date of receipt.

R. Failing to create adequate records, which shall be maintained for a period of three (3) years and made available to the Commission's staff for inspection and copying upon reasonable notice, from which the validity of any savings claims, retail price claims, comparative value claims, or other representations of the type described in Paragraphs II G(7), II M and II N of this order can be determined, and making any pricing claims within the scope of this provision unless there [24] are in existence for at least the six (6) months preceding such claims records from which the validity of such claims can be determined.

S. Failing to attach to any contract for the sale, rental or lease of any publication, merchandise, service or combination thereof a written statement that clearly and conspicuously discloses, and only discloses, the following information in the indicated order and manner:

(1) in 12-point boldface type size the terminology:

PRICE LIST

THE FOLLOWING PRICES ARE THE *ONLY* AUTHORIZED PRICES AT WHICH THE LISTED ITEMS MAY BE OFFERED. ANY PRICE NOT LISTED BELOW IS UNAUTHORIZED AND FALSE.

(2) a list of all publications, merchandise, services or combination thereof currently offered for sale, rental or lease, and in immediate conjunction thereto each price at which any respondent is authorized to offer said product or service pursuant to Paragraph II M of this order. [25]

(3) in 12-point boldface type the terminology, when applicable:

FREE ITEMS

ONLY THE FOLLOWING PRODUCTS AND SERVICES MAY BE OFFERED FREE. YOU ARE PAYING FOR ANY ITEMS RECEIVED AND NOT LISTED BELOW.

(4) a list of all publications, merchandise or services currently offered as free, without cost, or as a bonus pursuant to Paragraph II G(7) of this order.

T. Failing to orally instruct any person at the time said person signs any contract for sale, rental or lease, of any publication, merchandise, service or combination thereof, pursuant to an oral sales presentation, that a "Price List" is attached to said person's contract.

III

It is further ordered, That respondents Grolier, Incorporated, American Peoples Press, Inc., Americana Interstate Corp., Career Institute, Inc., Grolier Enterprises, Inc., and Grolier Reading Programs, Inc., corporations, and their successors or assigns, their officers, agents, representatives and employees, directly or indirectly, through any corporation, [26] subsidiary or division, or other device, in connection with the advertising, offering for sale, sale or distribution of any textbook, encyclopedia, reference or educational material, training course or teaching machine, or any other publication, merchandise or service through the use of any program, plan, method or device, that provides or purports to provide for the sale or distribution of any of said items to any person on an approval basis, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

A. Representing, directly or by implication, either orally or in writing that:

(1) any person has the option to receive each publication, merchandise or service, separately and individually, and to accept or reject same, unless such person is allowed in all instances to receive and to purchase or reject each such publication, merchandise or service separately and individually;

(2) any person will not receive any further publication, merchandise or service after the respondent concerned has received a timely notification of the person's cancellation of any such program, plan or method of sale [27] or distribution, unless such is the fact; or misrepresenting, in any manner, any consequence resulting from any person's cancellation of his participation in any such program, plan, or method of sale or distribution; and

(3) any person incurs no risk or obligation by joining or participating in any such program, plan, or method of sale or distribution; or misrepresenting, in any manner, any condition, right, duty or obligation imposed on any person.

B. Disseminating, or causing the dissemination of, any advertisement which fails to disclose in a clear and conspicuous manner:

(1) a description of the conditions and terms of any such program, plan, or method of sale or distribution, and the duties, risks and obligations of any subscriber thereto; and

(2) a description of each publication, merchandise or service to be offered for sale, the billing charge to be made therefor, the anticipated total number of publications, merchandise or [28] services included in any such program, plan or method of sale or distribution, the number of publications, merchandise or services that will be included in each shipment of such items, and the number of and the intervals between each such shipment.

C. Failing to disclose, clearly and conspicuously, on any return coupon, order form or any other document used for responding to any such program, plan, or method of sale or distribution, the following information:

(1) the anticipated total number of publications, merchandise or services included in any such program, plan, or method of sale or distribution;

(2) the number of publications, merchandise or services that will be included in each shipment of such items; and

(3) the number of and the intervals between each such shipment.

D. Failing to disclose, clearly and conspicuously, in immediate conjunction with any publication, merchandise, service or notice thereof sent to any subscriber [29] the anticipated date on which the respondent from whom the subscriber obtained any of such items will initiate processing of the next shipment of any such item.

E. Failing to provide to any person in conjunction with each notice of any shipment of any publication, merchandise or service, a clear and conspicuous means by which said person may exercise his option or right to cancel said shipment, if such is his right.

IV

It is further ordered, That respondents Grolier, Incorporated, American Peoples Press, Inc., Americana Corporation, Americana Interstate Corp., Federated Credit Corp., Career Institute, Inc., Grolier Interstate, Inc., Grolier New Era Corp., Madison Enterprises, Inc., R. H. Hinkley Company, Spencer International Press, Inc., The Grolier Society, Inc., and The Richards Company, corporations, and their successors, assigns, officers, agents, representatives and employees, directly or indirectly, through any corporation, subsidiary, division or other device, in connection with the collection or attempted collection of any debt allegedly due and owing pursuant to any contract or other agreement relating to the purchase or other receipt of any textbook, encyclopedia, [30] reference or educational material, training course or teaching machine, or any other publication, merchandise or service, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

A. Representing, directly or by implication, either orally or in writing that:

(1) any company, corporation, or entity engaged in collection of monies allegedly due or owing to such concerns or any other company, corporation or entity has separate *bona fide* departments or divisions for legal matters, unless such are the facts; or misrepresenting, in any manner, the existence, or functions of any division or department of any company, corporation or entity;

(2) the Code of Federal Regulations, or any other federal regulation or statute, provides that any employee of the Federal Government who has any outstanding debt due or owing may be subject to dismissal from the federal service for failure to pay said debt unless the respondent concerned can demonstrate that sufficient facts exist with regard to the [31] employee to whom the representation was made which establish the propriety of such claim;

(3) any person who utilizes the United States mail to obtain any

publication, merchandise or service and who fails to pay or becomes delinquent in paying for any such item will be subject to prosecution for mail fraud under federal law unless the respondent concerned can demonstrate that sufficient facts exist, with regard to person to whom the representation was made, which establish the propriety of such claim; or misrepresenting, in any manner, the rights, duties or obligations of any person arising from any federal, state, or local statute, ordinance, or regulation;

(4) any respondent utilizes the services of credit reporting companies or other entities for persons who disseminate credit information in a manner which will adversely affect the public or general credit rating of any person who has become delinquent in paying any debt unless the respondent concerned can demonstrate [32] that sufficient facts exist, with regard to the person to whom the representation was made, which establish the propriety of such claim, or misrepresenting, in any manner, that any person's public or general credit rating will be adversely affected;

(5) any letter, notice or other communication which has been prepared, originated or composed by any respondent has been prepared, originated or composed by any other person, firm or corporation;

(6) suit will be instituted to recover any delinquent debt, or that any delinquent debt will be transferred to any attorney with instructions to institute suit, or that any other legal step to collect any outstanding debt will be taken, unless a definite date is set forth for such action and such are the facts; or misrepresenting, in any manner, respondents' relationship with, or instructions to, any attorney, or the course of action that will be taken by any attorney or misrepresenting in any manner that any account has been transferred to any [33] person or entity for collection unless those are the facts.

B. Using any correspondence forms or any written materials which appear to depict official legal process.

V

For the purpose of the following provisions of this order, the term "respondents" shall apply to each of the respondents named in Paragraph I and II of the order.

It is further ordered, That respondents:

A. Deliver by registered mail, a copy of this decision and order to each of their salesmen, agents, solicitors, or other persons engaged by respondents for the promotion, sale or distribution of any of the publications, merchandise or services included in this order, and to any person engaged by respondents to perform such duties in the future at the time such person is so engaged;

B. Obtain from each person described in Paragraph V A, a signed statement setting forth their intention to conform their business practices to the requirements of this order; retain said statement during the period of three (3) years thereafter; and make said statement available to the Commission's staff for inspection and copying upon reasonable notice; [34]

C. Advise each such present and future salesman, agent, solicitor, or other person engaged by respondents for the promotion, sale or distribution of any of the publications, merchandise or services included in this order that respondents will terminate the engagement or services of any such person, unless such person agrees to and does furnish to respondents a statement required by Paragraph V B, above; and

D. If any such person will not agree to file a statement with respondents as required by Paragraph V B above, and be bound by the provisions of this order, the respondents shall immediately terminate the services of such person.

E. Furnish the Commission on a quarterly basis with a list, including business addresses, of those independent or outside distributors who have purchased or otherwise obtained for resale any of the publications, merchandise or services included in this order.

VI

It is further ordered, That the respondent shall forthwith distribute a copy of this order to each of their operating divisions. [35]

VII

It is further ordered, That respondents shall notify the Commission at least thirty (30) days prior to any proposed change in any of the corporate respondents such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of which may affect compliance obligations arising out of this order.

VIII

It is further ordered, That respondents shall, within sixty (60) days after the effective date of this order, file with the Commission a report in writing setting forth in detail, the manner and form in which they have complied with this order.

APPENDIX A

NOTICE

Attached hereto are the *pertinent provisions* of a cease and desist order entered against Grolier, Incorporated and certain of its subsidiaries, including Grolier Interstate, Inc. by the Federal Trade Commission, an agency of the Federal Government. Violation of any provision of this order can result in severe monetary penalties to Grolier, Incorporated and Grolier Interstate, Inc. If you are employed by Grolier, Incorporated or any of its subsidiaries, you will be *required* to observe the provisions of this order. Violation of any provision of this order by an employee constitutes a violation of a federal law.

You should carefully read this order before agreeing to any employment arranged with Grolier, Incorporated or any of its subsidiary companies.

(President)
Grolier, Incorporated

IN THE MATTER OF

FORD MOTOR COMPANY, ET AL.

Docket 9073. Interlocutory Order, Mar. 16, 1978

Denial of a respondent's application for interlocutory review of ALJ's denial to stay the proceedings and to consider other motions.

ORDER DENYING APPLICATION FOR REVIEW

On March 15, 1978, respondent Francis Ford, Inc., filed a document styled "Emergency Petition for Review to the Federal Trade Commission" which we will treat as an application for interlocutory review of the ALJ's ruling on March 13, 1978, denying respondent's motion to stay the proceedings and to consider other motions.[1] The ALJ also denied a request to certify his order to the Commission under Section 3.23(b) of the Commission's Rules of Practice, 16 C.F.R. 3.23(b).

Section 3.23(a) of the Commission's Rules of Practice specifies the limited situations in which an interlocutory appeal from a ruling of the ALJ will be entertained in the absence of certification by the ALJ uner Section 3.23(b).[2] Respondent has advanced no basis on which an appeal will lie under one of the enumerated subsections.

Even if the order were subject to interlocutory review under Section 3.23, it would be reversible only if there had been a clear abuse of discretion by the ALJ. *Kellogg Co., et al.*, 83 F.T.C. 1956 (1974) and 86 F.T.C. 650 (1975). Insofar as the respondent seeks a delay of the proceedings, the Commission has repeatedly ruled that matters of scheduling are within the sound discretion of the law judge. *See, e.g., Maremont Corp.*, 77 F.T.C. 1654 (1970); *American Home Products*, Dkt. 8918, Order of August 18, 1977 Denying Application

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[1] Respondent submitted the following motions to the ALJ:

Motion for Emergency Determination on Motion to Withdraw Matter from Adjudication for the Purpose of Considering Such Respondent's Proposed Consent Agreement and on its Motion in Opposition to Withdrawal of Ford Motor Company and Ford Motor Credit Company from this proceeding or in the Alternative to Join Such Respondents as Third Party Respondents;

Motion to Withdraw the Matter from Adjudication for the Purpose of Considering Respondent's Proposed Consent Agreement, for Certification of Settlement Proposal, and for a Stay of the Proceedings;

Motion in Opposition to Withdrawal of Ford Motor Company and Ford Motor Credit Company from Proceeding or in the Alternative to Join Such Respondents as Third Party Respondents.

[2] Section 3.23(a) of the Commission's Rules of Practice provides that

"The Commission may, in its discretion, entertain interlocutory appeals where a ruling of the Administrative Law Judge: (1) requires the disclosure of the Commission records or the appearance of an official or employee of the Commission pursuant to §3.26; (2) requires the appearance of other government officials pursuant to §3.37; (3) suspends an attorney from participation in a particular proceeding pursuant to §3.42(d); or (4) grants or denies an application for intervention pursuant to the provisions of §3.14."

for Review at 2 [90 F.T.C. 148]. Insofar as respondent requests a review of the ALJ's refusal to rule on respondent's other motions, its request is premature.

***It is therefore ordered,* That the application is denied.**

IN THE MATTER OF

VERRAZZANO TRADING CORPORATION, ET AL.

Docket 9038. Interlocutory Order, Mar. 17, 1978

Order directing the filing of a memorandum and answer thereto setting forth further arguments as to unconstitutionality of certain provisions of the Wool and Textile Acts.

ORDER WITH RESPECT TO BRIEFING OF CONSTITUTIONAL ISSUES

In preparation for oral argument in this matter, the Commission has noted that respondents take the position in their appeal brief that certain provisions of the Wool Products Labeling Act, 15 U.S.C. 68 and the Textile Fiber Products Identification Act, 15 U.S.C. 70 are unconstitutional insofar as they may require posting of a bond as a condition of continued importation by an importer found to have violated the Acts.

Respondents contend that they did not argue the constitutional issue before the administrative law judge because of his alleged position that the constitutional issue was not a proper one for consideration by the agency, a position that complaint counsel have maintained in their reply brief. Respondents contend that this matter should be remanded to the administrative law judge to consider their constitutional arguments.

While the Commission has made no final determination with respect to the contentions raised by the parties in their briefs regarding whether or not the Commission should review the constitutionality of laws it enforces, the Commission does believe that the constitutional issue is a question of law and can be adequately considered by the Commission if it determines to take it up, upon written briefs, without the need for further proceedings before an administrative law judge.[1] Accordingly, respondents should submit within 20 days from the date of this order a memorandum setting forth their constitutional arguments, if they desire that such further arguments be considered by the Commission. Complaint counsel shall respond within 15 days. Therefore,

It is ordered, That if respondents desire that the Commission consider further arguments as to the unconstitutionality of certain provisions of 15 U.S.C. 68 and 15 U.S.C. 70, they shall file a memorandum within 20 days of service of this order setting forth such further arguments. Complaint counsel shall thereupon file an answer within 15 days of receipt of respondents' memorandum.

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[1] In reaching this determination the Commission has reviewed respondents' Motion received May 17, 1976; complaint counsel's "Reply to Respondents' Motion for a Subpoena Duces Tecum" received June 2, 1976; complaint counsel's "Motion to Strike" received May 18, 1976; respondents' reply thereto received June 14, 1976; respondents' "Reply to Complaint Counsel's Reply. . ." dated June 21, 1976; and Judge Teetor's "Ruling on Motion to Strike" of July 14, 1976.

IN THE MATTER OF

JOHNSON PRODUCTS COMPANY, INC.

MODIFIED ORDER, IN REGARD TO ALLEGED VIOLATION OF SECS. 5 AND 12 OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2788. Complaint, Feb. 10, 1976 — Modified Order, Mar. 20, 1978

This order modifies a consent order issued February 10, 1976, 41 FR 11172, 87 F.T.C. 206, which was remanded to the Commission for reconsideration by the Court of Appeals for the Seventh Circuit. Modifications in the order exclude references to the advertising firm, restrict provisions of the order to hair straightening products, and are designed to eliminate the significant differences between the original order and that of a competitive company *(Revlon, Inc.)*.

ORDER MODIFYING ORDER TO CEASE AND DESIST

On February 10, 1976 the Commission rejected an attempt by respondent Johnson Products Co., Inc. to withdraw from an executed consent order agreement and, on that date, the Commission entered a final cease and desist order. Thereafter, respondent petitioned the Court of Appeals for the Seventh Circuit to review and set aside the order, contending, *inter alia,* that the Commission patently abused its discretion by refusing to permit respondent to withdraw from the consent agreement in the face of its claim that the Commission had engaged in an "unfair and arbitrary discrimination between similarly situated competitors. . ." (*i.e.,* Revlon, Inc. and respondent). The Court stayed enforcement of the order and remanded the matter to the Commission, noting the prospect that the proceeding might be reopened and modified to eliminate some or all of the critical disparities between the *Revlon* and *Johnson* orders.

After extended negotiations, the parties executed an agreement, which will be treated as a petition to reopen this proceeding, containing an order to cease and desist. The modifications contained in this agreement substantially eliminate the significant differences between the *Revlon* and *Johnson* orders.

The Commission has duly considered the modifications encompassed in the agreement and has determined that the order should be so modified. Accordingly,

It is ordered, That the proceeding be, and it hereby is, reopened.

It is further ordered, That the order to cease and desist, as it applies to respondent Johnson Products Company, Inc., be, and it hereby is, modified by striking the section entitled "Order" and substituting therefor the following:

ORDER

I. *It is ordered,* That respondent Johnson Products Company, Inc., a corporation, its successors and assigns, and its officers, agents, representatives and employees, directly or through any corporation, subsidiary, division or other device, in connection with the advertising, offering for sale, sale, or distribution of Ultra Sheen Creme Relaxer (Ultra Sheen Relaxer) or any hair care product in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, do forthwith cease and desist from:

A. Representing in writing, orally, visually, or in any other manner, directly or by implication, that:

1. Any hair straightening product is comfortable, gentle or safe.
2. Any hair straightening product is easy to use or to apply.
3. Any hair straightening product feels cool to skin or scalp.

B. Representing, in any manner, directly or by implication, the efficacy of any hair straightening product or the ingredients therein, unless, at the time such representation is made, respondent has in its possession a reasonable basis, consisting of competent and reliable controlled tests to support such representation; or misrepresenting in any manner the nature of any such product or its ingredients or the effect of any such product or its ingredients on hair or skin or any other structure of the body.

C. Representing, in any manner, directly or by implication, the safety of any hair care product or the ingredients therein, unless at the time such representation is made, respondent has in its possession a reasonable basis, consisting of competent and reliable controlled tests, to support such representation. For purposes of this provision, failure to disclose facts shall not constitute a representation.

D. Disseminating or causing to be disseminated any advertisement of Ultra Sheen Relaxer or any hair straightening product of similar composition, which fails to disclose, clearly and conspicuously, with nothing to the contrary or in mitigation thereof, the following statement exactly as it appears below:

> WARNING: Follow directions carefully to avoid skin and scalp irritation, hair breakage and eye injury.

II. *It is further ordered,* That respondent Johnson Products Company, Inc., a corporation, its successors and assigns, and its officers, agents, representatives and employees, directly or through any corporation, subsidiary, division or other device, in connection with the advertising, offering for sale, sale, or distribution of Ultra Sheen Relaxer or any hair care product, do forthwith cease and desist from:

A. Disseminating or causing to be disseminated by United States mail or by any means in or having an effect upon commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, for the purpose of inducing or which is likely to induce, directly or indirectly, the purchase of any such product, any advertisement which contains a representation prohibited by Paragraph I of this order or which omits a disclosure for such product required by Paragraph I of this order.

B. Disseminating or causing to be disseminated by any means, for the purpose of inducing or which is likely to induce, directly or indirectly, the purchase of any such product in or having an effect on commerce as "commerce" is defined in the Federal Trade Commission Act, as amended, any advertisement which contains a representation prohibited by Paragraph I of this order or which omits a disclosure for such product required by Paragraph I of this order.

III. *It is further ordered,* That respondent Johnson Products Company, Inc., a corporation, its successors and assigns and its officers, agents, representatives and employees, directly or through any corporation, subsidiary, division or other device in connection with the offering for sale, sale, or distribution of Ultra Sheen Relaxer or any hair straightening product of similar composition in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, do forthwith cease and desist from failing to include clearly and conspicuously on the information panel of the product package (*i.e.,* the package containing the immediate container of the professional or home use hair straightening product), on the package insert, and on the label of the relaxer container of any such product, with nothing to the contrary or in mitigation thereof, the following disclosures exactly as they appear below:

WARNING:

1. This product contains sodium hydroxide (lye). You must follow directions carefully to avoid skin and scalp burns, hair loss, and eye injury.

2. Do not use if scalp is irritated or injured.

3. Do not use on bleached hair. Do not use on permanently colored hair which is breaking, splitting or otherwise damaged. For hair that has been permanently colored and shows no sign of damage, use only mild strength formula.

4. If you have previously relaxed your hair, relax only the new growth, as described in the directions.

5. If the relaxer causes skin or scalp irritation, rinse out immediately and wash with shampoo in the kit. If irritation persists or if hair loss occurs, consult a physician.

6. If the relaxer gets into eyes, rinse immediately and consult a physician.

Provided, however, that if such hair straightening product is offered for sale, sold or distributed without a neutralizing shampoo, respondent will disclose the following in place of Warning No. 5 above:

5. If the relaxer causes skin or scalp irritation, rinse out immediately and wash with a non-alkaline shampoo (ph below 7). If irritation persists, or if hair loss occurs, consult a physician.

Provided further, however, that respondent may use existing retail product packages, package inserts, and container labels if such packages, inserts and labels conform to the order entered in this matter on February 10, 1976.

IV. *It is further ordered,* That respondent shall distribute a copy of this order to its present and future officers, directors, and operating division and that respondent secure from each such person a signed statement acknowledging receipt of the order.

V. *It is further ordered,* That respondent maintain complete business records relative to the manner and form of its continuing compliance with the terms and provisions of this order. Each record shall be retained by respondent for at least three years after it is made.

VI. *It is further ordered,* That respondent notify the Commission at least thirty days prior to any proposed change in respondent, such as dissolution, assignment or sale resulting in the emergence of a successor corporation or corporations, the creation or dissolution of subsidiaries, a change in the corporate name or address, or any other change in the corporation which may affect compliance obligations arising out of this order.

VII. *It is further ordered,* That the respondent herein shall, within sixty (60) days after service of this order, file with the Commission a written report setting forth in detail the manner and form of its compliance with this order; *provided, however,* that such compliance report need not contain materials or information previously submitted to the Commission to demonstrate compliance with the order entered in this matter on February 10, 1976.

IN THE MATTER OF

FERRARA IMPORTS, LTD., ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION AND WOOL PRODUCTS LABELING ACTS

Docket C-2918. Complaint, Mar. 24, 1978—Decision, Mar. 24, 1978

This consent order, among other things, requires a New York City importer and manufacturer of men's clothing to cease misrepresenting, or failing to affix to their products, required fiber disclosure labels. The firm is additionally required to furnish affected customers with a copy of the order.

Appearances

For the Commission: *Jerry R. McDonald.*

For the respondents: *Melvin Kynter,* New York City.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, as amended, and the Wool Products Labeling Act of 1939, and by virtue of the authority vested in it by said Acts, the Federal Trade Commission, having reason to believe that Ferrara Imports, Ltd., a corporation, and Louis Ferrara, individually and as an officer of said corporation, hereinafter sometimes referred to as respondents, have violated the provisions of said Acts and the rules and regulations promulgated under the Wool Products Labeling Act of 1939, and it now appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent Ferrara Imports, Ltd. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York with its principal office and place of business located at 655 Madison Ave., New York, New York.

Respondent Louis Ferrara is an officer of the corporate respondent. He formulates, directs and controls the acts and practices of the corporate respondent including the acts and practices hereinafter set forth. His address is the same as that of the corporate respondent.

Respondents are engaged in the business of manufacturing men's clothing, including but not limited to men's suits, and the sale and distribution of said items of clothing.

PAR. 2. Respondents, now and for some time last past, have imported for introduction into commerce, introduced into commerce, sold, transported, distributed, delivered for shipment, shipped, and offered for sale, in commerce, as "commerce" is defined in the Wool Products Labeling Act of 1939, wool products as "wool product" as defined therein.

PAR. 3. Certain of said wool products were misbranded by respondents within the intent and meaning of Section 4(a)(1) of the Wool Products Labeling Act of 1939 and the rules and regulations promulgated thereunder, in that they were falsely and deceptively stamped, tagged, labeled, or otherwise identified with respect to the character and amount of the constituent fibers contained therein.

Among such misbranded wool products, but not limited thereto, were samples, swatches or specimens used to effect sales of certain wool blend men's suits stamped, tagged, labeled or otherwise identified by respondents as "35% wool, 50% polyester and 15% other fibers," whereas, in truth and in fact, said products contained substantially different fibers and amounts of fibers than represented.

PAR. 4. Certain of said wool products were further misbranded by respondents in that they were not stamped, tagged, labeled, or otherwise identified as required under the provisions of Section 4(a)(2) of the Wool Products Labeling Act of 1939 and in the manner and form as prescribed by the rules and regulations promulgated under said Act.

Among such misbranded wool products, but not limited thereto, were wool products, namely samples, swatches or specimens used to effect sales of wool blend men's suits, with labels on or affixed thereto, and wool blend men's suits, with no labels on or affixed thereto, which failed to disclose the percentage of the total fiber weight of the said wool products, exclusive of ornamentation not exceeding 5 per centum of said total fiber weight, of (1) wool, (2) reprocessed wool, (3) reused wool, (4) each fiber other than wool, when said percentage by weight of such fiber is 5 per centum or more, and (5) the aggregate of all other fibers.

PAR. 5. The acts and practices of the respondents as set forth above were, and are, in violation of the Wool Products Labeling Act of 1939 and the rules and regulations promulgated thereunder, and constituted, and now constitute, unfair methods of competition and unfair and deceptive acts and practices, in or affecting commerce, under the Federal Trade Commission Act, as amended.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondents named in the caption hereof, and the respondents having been furnished thereafter with a copy of a draft of complaint which the New York Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with violation of the Federal Trade Commission Act, as amended, and the Wool Products Labeling Act of 1939; and,

The respondents and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and,

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondents have violated the said Acts, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent Ferrara Imports, Ltd. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York, with its office and principal place of business located at 655 Madison Ave., New York, New York.

Respondent Louis Ferrara is an officer of said corporation. He formulates, directs and controls the policies, acts and practices of said corporation, and his address is the same as that of said corporation.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents and the proceeding is in the public interest.

ORDER

It is ordered, That respondents Ferrara Imports, Ltd., a corporation, its successors and assigns, and its officers, and Louis Ferrara, individually and as an officer of said corporation, and respondents' representatives, agents, and employees, directly or through and corporation, subsidiary, division or any other device, in connection with the introduction or importing for introduction, or manufacture for introduction, into commerce, or the offering for sale, sale, transportation, distribution, delivery for shipment or shipment, in commerce, of wool products as "commerce" and "wool product" are defined in the Wool Products Labeling Act of 1939, do forthwith cease and desist from misbranding such products by:

1. Falsely and deceptively stamping, tagging, labeling, or otherwise identifying such products.
2. Failing to securely affix to or place on, each such product a stamp, tag, label, or other means of identification showing in a clear and conspicuous manner each element of information required to be disclosed by Section 4(a)(2) of the Wool Products Labeling Act of 1939.

It is further ordered, That respondents mail a copy of this order to each of their customers that purchased the wool products which gave rise to this complaint.

It is further ordered, That respondents notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance obligations arising out of the order.

It is further ordered, That the individual respondent named herein promptly notify the Commission of each change in business or employment status, which includes discontinuance of his present business or employment and each affiliation with a new business or employment, for ten (10) years following the effective date of this order. Such notice shall include respondent's current business address and a description of the business or employment in which he is engaged as well as a description of his duties and responsibilities. The expiration of the notice provision of this paragraph shall not affect any other obligations arising under this order.

It is further ordered, That the respondents herein shall within sixty (60) days after service upon them of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied with this order.

IN THE MATTER OF

JIM WALTER CORPORATION

Docket 8986. Interlocutory Order, Mar. 30, 1978

Denial of respondent's petition for reconsideration of final order and accompanying opinion, for reopening the proceeding for issuance of an environmental impact statement, for tolling statutory time for filing petition for review, and for oral argument.

ORDER DENYING PETITION FOR RECONSIDERATION AND OTHER RELIEF

Respondent, Jim Walter Corporation ("Jim Walter") has filed a petition for reconsideration of the Commission's Final Order and accompanying Opinion, for reopening the proceeding to receive certain affidavits, for issuance of an environmental impact statement, for tolling the statutory time for filing a petition for review in the court of appeals, and finally, for oral argument on these issues.

Jim Walter's petition for reconsideration seeks modification of the Commission's Final Order so that it may retain Carey-Canadian Mines, Ltd. ("Carey-Canadian"), a Canadian subsidiary of Panacon Corporation ("Panacon"), engaged in the mining of asbestos fiber, as well as the Philip Carey Division plant at Elizabethtown, Kentucky, which is engaged in the manufacture of urethane foam insulation.

The threshold question which must be faced in connection with a petition for reconsideration filed pursuant to Rule 3.55 is whether the petition raises issues which petitioner had a prior opportunity to address before the Commission. Respondent has been on notice since the commencement of this proceeding that, if liability were found, effective relief might encompass divestiture of all of the Panacon assets acquired by the Celotex Corporation.[1] Allowing respondent yet another opportunity to suggest an appropriate remedy in this case would serve to bifurcate the Commission's adjudicative proceedings into a liability phase, concluding upon issuance of a final order, and a remedy phase, commencing with a petition for reconsideration. Hence, for reasons of administrative efficiency and fairness to all parties, respondent's petition for reconsideration and for reopening of the record may be denied as not in accordance with Rule 3.55.

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[1] The Administrative Law Judge's order would have required respondent to divest all of the assets of the Philip Carey Division of Panacon, including the Elizabethtown plant. I.D. P. 64-65. Although the Law Judge did not order divestiture of Carey-Canadian, complaint counsel urged on appeal that the Commission order divestiture of Celotex's new Goldsboro plant, as well as all Panacon assets, including Carey-Canadian. CAB at 26-27. Thus, respondent has been on notice from the onset of this litigation that Carey-Canadian might be divested and of possible obstacles to such divestiture, stemming from Canada's Foreign Investment Review Act, 21-22 Eliz. II, c. 46 (Can.), which was enacted on September 12, 1973, more than ten months prior to the issuance of the complaint.

Even considering the merits of respondent's petition, our decision remains the same. Only restoration of a viable competitive entity can mitigate the substantial harm to competition brought about by respondent's acquisition. As we have recently emphasized in a related context, the Commission must typically rely upon an inference that the acquired firm, which was a viable entity prior to its acquisition, is likely to be an effective future competitor after divestiture. *Fruehauf Corporation, Inc.*, Dkt. No. 8972 (Slip Op. at 35–36) (Feb. 22, 1978 [91 F.T.C. 132]); *RSR Corporation*, 88 F.T.C. 873, 894 (1976). Since the passage of time might weaken this inference, it is essential that divestiture incorporate all additions and improvements made to the original assets. That the Elizabethtown plant was under construction by Philip Carey at the time of the acquisition and had not yet begun operations is therefore of little consequence. Its value to a healthy, independent Philip Carey must be presumed in the absence of convincing proof to the contrary.

With respect to Carey-Canadian, Jim Walter highlights in its petition the percentage of Carey-Canadian sales to Philip Carey roofing plants. While such data is clearly material to formulation of an effective remedy, (see Commission Opinion at 49), it only represents part of the picture. As we noted previously, the Philip Carey division has purchased as much as 40 to 55 percent of its fiber needs from Carey-Canadian. Since most of this asbestos is apparently utilized for production of asphalt and tar roofing products, divestiture of Carey-Canadian is necessary to insure Philip Carey's ready access to supply of an essential raw material in addition to its successful reinstatement as a vigorous competitor in the product market found relevant in this case.[3]

Petitioner further argues that divestiture of Carey-Canadian cannot be accomplished without the approval of the Canadian Government and that political developments in the Province of Quebec, including the threat of nationalization, will be a "substantial negative factor" for prospective purchasers. We do not understand Jim Walter to contend that divestiture of Carey-Canadian is impossible, only that it cannot be accomplished in a facile manner. It is clearly inappropriate at this time to prognosticate on the likelihood of finding a Canadian purchaser for the subject assets or on the possibility of obtaining Canadian approval in the event a non-Canadian purchaser is found. Any insurmountable difficulties which do arise are best considered in the context of compliance.

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[3] Even if the percentage of Philip Carey's output attributed to asphalt and tar roofing products utilizing asbestos is relatively small, the contribution to profit may be proportionately greater. And, of course, that does not take into account Carey-Canadian's own substantial contribution to the viability of Panacon prior to the acquisition by Jim Walter. (*See* CX–39–0)

Jim Walter has also petitioned the Commission for issuance of a detailed environmental impact statement or a statement as to why an environmental impact statement is not required. In support of its petition, respondent argues that the Commission's order could result in violation of antipollution laws in the event respondent divests to a "notorious polluter." At the outset, we do not believe an environmental impact statement need be prepared in connection with an order issued in an adjudicative proceeding. See Rule 1.82(d). Even were that rule inapplicable, we find nothing here to justify the filing of an impact statement.

Respondent's argument necessarily requires several difficult assumptions. We are required first to assume that potential purchasers will violate the law and second that Federal, state, and local environmental agencies are powerless to prevent transgressions of the law. We are also asked to assume that Jim Walter would divest to such a purchaser and that the Commission would concur in the transaction.

Further, a review of the case law confirms our view that the Commission's order cannot by any stretch of the imagination be characterized as a "major Federal action significantly affecting the quality of the human environment" 42 U.S.C. 4332(2)(c)(1970). The order here represents a partial return to the status quo existing prior to the acquisition. And like divestiture orders generally, the order affects only the ownership of existing plants and facilities; it does not necessarily entail the creation of new capacity or the consumption of additional environmental resources. *See Gifford-Hill & Co., Inc* v. *FTC,* 389 F. Supp.167, 175 (D.D.C. 1974), *aff'd,* 523 F.2d 730 (D.C. Cir. 1975); *National Ass'n of Gov't Employees* v. *Rumsfeld,* 413 F. Supp. 1224, 1229–30 (D.D.C. 1976); *Duke City Lumber Co.* v. *Baty,* 382 F. Supp. 362, 375 (D.D.C. 1974), *aff'd in part,* 539 F.2d 220 (D.C. Cir. 1976).

It is ordered, therefore, that respondent's petition for reconsideration of the Final Order and accompanying Opinion in this proceeding for reopening the proceeding for issuance of an environmental impact statement, for tolling the statutory time for filing a petition for review, and for oral argument is hereby denied.

Chairman Pertschuk did not participate.

IN THE MATTER OF

THE COCA-COLA COMPANY, ET AL.

ORDER, OPINION, ETC., IN REGARD TO ALLEGED VIOLATION OF SECTION 5 OF THE FEDERAL TRADE COMMISSION ACT

Docket 8855. Complaint, July 15, 1971 — Final Order, April 7, 1978

This order, among other things, requires an Atlanta, Ga. soft drink manufacturer and three parent bottlers to cease imposing in any manner territorial limitations or class of customer restrictions on its licensed Coca-Cola or allied product bottlers, in connection with the sale or distribution of soft drink products sold in other than refillable containers. The firm is additionally required to provide protection for confidential information submitted by its bottlers.

Appearances

For the Commission: *Raymond L. Hays, Martin A. Rosen, Duncan J. Farmer, Michael J. Bloom* and *Jeffrey F. Shaw.*

For the respondents: *Gordon B. Spivack, Harry G. Sklarsky* and *Thomas D. Brislin, Lord, Day & Lord,* New York City.

J. Guy Beatty, Jr., Miller, Martin, Hitching, Tipton, Lenihan & Waterhouse, Chattanooga, Tenn. for Coca-Cola Bottling Co. (Thomas), Inc. and Coca-Cola Bottling Works (Thomas), Inc.

For the intervenors: *Willis B. Snell, William M. Hames, Michael L. Denger, Stephen S. Cowen* and *Robert W. Clark, III, Sutherland, Asbill & Brennan,* Washington, D.C. for The Coca-Cola Bottlers' Association, The Scioto Coca-Cola Bottling Company, Roddy Manufacturing Company, Elberton Coca-Cola Bottling Company, Westminster Coca-Cola Bottling Company, Inc. and Texas Coca-Cola Bottling Company.

Thomas Matthews, Wald, Harkrader & Ross, Washington, D.C. for Coca-Cola Bottling Company of Los Angeles, Quaker State Coca-Cola Bottling Co. and Detroit Coca-Cola Bottling Company.

Bartlett H. McGuire, Davis, Polk & Wardwell, New York City for The Coca-Cola Bottling Company of New York.

Theodore Kleinman, Zuckert, Scoutt & Rasenberger, Washington, D.C. for Associated Coca-Cola Bottling Co.

John P. Gaither, Witt, Gaither, Richardson, Henniss & Whitaker, Chattanooga, Tenn. for Consolidated Coca-Cola Bottling Co.

Robert N. Nanovic, Nanovic & McKinley, Jim Thorpe, Pa. for Coatesville Coca-Cola Bottling Works, Inc.

William H. Sanders, Blackwell, Sanders, Matheny, Weary & Lombardi, Kansas City, Mo. for The Coca-Cola Bottling Company of Mid-America.

Joe A. Walters, O'Conner & Hannan, Minneapolis, Minn. for Coca-Cola Bottling Midwest, Inc.

COMPLAINT

The Federal Trade Commission, having reason to believe that the parties named in the caption hereof, each of which is hereby made and is sometimes hereinafter referred to as respondent(s), have violated the provisions of Section 5 of the Federal Trade Commission Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint, stating its charges in this respect as follows:

PARAGRAPH 1. For the purposes of this complaint, the following definitions shall apply:

(a) Bottler – any individual, partnership, corporation, association, or other business or legal entity which purchases respondents' concentrate for use in the manufacture and sale, primarily at wholesale, of respondents' pre-mix or post-mix syrups or soft drink products, or who purchases respondents' pre-mix or post-mix syrups or soft drink products for resale, primarily at wholesale;

(b) Central warehousing – a method of distribution in which soft drink products are received at a storage facility and either resold or delivered to retail outlets or wholesalers;

(c) Concentrate – the basic soft drink ingredient sold to bottlers by respondent, usually as a syrup, and which is combined with water and other ingredients for packaging in bottles or cans for sale and distribution as soft drink products, or is used to make post-mix and pre-mix syrups; [2]

(d) Consignment – a form of distribution in which the consignor retains title, dominion, bears all risks of loss and delivers his products to the consignee who is indistinguishable from a salesman or agent;

(e) Place of business – the location of any facilities available to a bottler without regard to customers or geographic area for production or service in the conduct of business operations, to include but not limited to business headquarters, branch sales offices, warehouses and garages, but specifically excluding the plant at which a bottler combines concentrate with water, and possibly other ingredients, for the packaging of soft drink products;

(f) Post-mix syrup – soft drink concentrate which is used in fountain dispensing or vending equipment and is usually sold by bottlers in steel tanks. A typical post-mix system draws one ounce of syrup from a tank, usually having about a five-gallon capacity, and mixes it at the point of sale with five ounces of carbonated water to produce approximately 600 six-ounce finished soft drink servings per tank;

(g) Pre-mix syrup – although essentially the same syrup as post-mix, a pre-mix system differs from a post-mix system in that it draws from a tank, usually having about a five-gallon capacity, a finished serving of soft drink product containing both syrup and carbonated water, "pre-mixed," to produce a 100 six-ounce soft drink servings per tank; and

(h) Soft drink products – nonalcoholic beverages and colas, carbonated and uncarbonated, flavored and non-flavored, sold in bottles and cans, or through pre-mix and post-mix systems or the like.

PAR. 2. Respondent The Coca-Cola Company, sometimes hereinafter referred to as Coca-Cola, is a corporation organized, existing and conducting its business under and pursuant to the laws of the State of Delaware. It maintains its office and principal place of business at 310 North Ave., N.W., Atlanta, Georgia. The Coca-Cola Company and subsidiaries had net sales of $1,185,808,864 (approximately 45 percent of which is accountable to foreign operations), and assets of $802,100,548 in 1968. In 1968, Coca-Cola made sales to over 900 domestic bottlers located throughout the United States. [3]

Respondent Coca-Cola Bottling Co. (Thomas), Inc., sometimes hereinafter referred to as Thomas Company, is a corporation organized, existing and conducting its business under and pursuant to the laws of the State of Delaware. It maintains its office and principal place of business at 1600 American Bank Building, Chattanooga, Tennessee. In 1968, Thomas Company made sales to over 196 bottlers located principally in Indiana, Maryland, Mississippi, New Jersey, New York, Ohio, Pennsylvania, Virginia and West Virginia.

Respondent Coca-Cola Bottling Works (Thomas), Inc., sometimes hereinafter referred to as Thomas Works, is a corporation organized, existing and conducting its business under and pursuant to the laws of the State of Delaware. It maintains its office and principal place of business at 1600 American Bank Building, Chattanooga, Tennessee. In 1968, Thomas Works made sales to over 65 bottlers located principally in the States of Kentucky and Tennessee.

Respondent Coca-Cola Bottling Works 3rd, Inc., sometimes hereinafter referred to as Works 3rd, is a corporation organized, existing and conducting its business under and pursuant to the laws of the State of Delaware. It maintains its office and principal place of business at 1600 American Bank Building, Chattanooga, Tennessee. In 1968, Works 3rd made sales to over 25 bottlers located principally in the States of Pennsylvania and New Jersey.

PAR. 3. Respondent Coca-Cola, through its Coca-Cola U.S.A. division, is engaged principally in the manufacture and sale of soft drink products and concentrate which it sells to over 900 bottlers who purchase the concentrate under a license to produce and sell soft drink products under such trade names of respondent Coca-Cola as "Coca-Cola" ("Coke"), "TAB," "Sprite," "Fresca," "Fanta" and "Simba." Bottlers combine the concentrate with water and other ingredients and package the mixture in bottles and cans for resale as soft drink products to retailers. In addition to manufacturing and selling soft drink products and concentrate to its bottlers, Coca-Cola operates bottling plants in 27 areas of the United States and sells soft drink products to retailers. [4]

Respondent Thomas Company has operated for many years as a parent bottler under an agreement with Coca-Cola by which Thomas Company was granted certain rights from Coca-Cola with respect to the sale of Coca-Cola soft drink products in certain designated territories. Thomas Company is engaged principally in the purchase of concentrate from Coca-Cola for resale by Thomas Company to numerous bottlers which have obtained licenses from it to bottle and resell certain specified trade name soft drink products of Coca-Cola.

Respondent Thomas Works has operated for many years as a parent bottler under an agreement with Coca-Cola by which Thomas Works was granted certain rights from Coca-Cola with respect to the sale of Coca-Cola soft drink products in certain designated territories. Thomas Works is engaged principally in the purchase of concentrate from Coca-Cola for resale by Thomas Company to numerous bottlers which have obtained licenses from it to bottle and resell certain specified trade name soft drink products of Coca-Cola.

Respondent Works 3rd has operated for many years as a parent bottler under an agreement with Coca-Cola by which Works 3rd was granted certain rights from Coca-Cola with respect to the sale of Coca-Cola soft drink products in certain designated territories. Works 3rd is engaged principally in the purchase of concentrate from Coca-Cola for resale by Works 3rd to numerous bottlers which have obtained licenses from it to bottle and resell certain specified trade name soft drink products of Coca-Cola.

PAR. 4. Respondents are engaged in "commerce" within the meaning of the Federal Trade Commission Act (15 U.S.C. 44) in that a continuous flow of interstate commerce in concentrate and soft drink products exists between their headquarters and production facilities and the numerous bottlers located throughout the United States which purchase their products.

PAR. 5. In the course and conduct of their businesses, respondents, except to the extent limited by the acts, practices and methods of competition hereinafter alleged, have been and are now in competition with other corporations, firms, partnerships and persons engaged in the manufacture, processing, distribution and sale of concentrate and soft drink products in commerce.

PAR. 6. Respondents have hindered, frustrated, lessened and eliminated competition in the distribution and sale of pre-mix and post-mix syrups and soft drink products [5] sold under their trade names by restricting their bottlers from selling outside of a designated geographical area. This restriction is set forth in the agreement between respondents and their bottlers.

A typical license between respondent Coca-Cola and its bottlers provides that as to a specifically described geographic territory:

> . . . COMPANY agrees to furnish to BOTTLER, and only to furnish for the territory herein referred to, sufficient syrup for bottling purposes to meet the requirements of BOTTLER in the territory herein described.
>
> * * * * * * *
>
> . . . COMPANY does hereby select BOTTLER as its sole and exclusive customer and licensee for the purpose of bottling the Bottlers' bottle syrup, COCA-COLA, in the territory described.
>
> [BOTTLER agrees] . . . not to use trade-marks COCA-COLA or COKE, nor bottle nor vend said product except in the territory herein referred to. This limitation, however, is not to prevent BOTTLER from acquiring similar rights for other territory.
>
> * * * * * * *
>
> [BOTTLER agrees] . . . not to use said distinctive [COCA-COLA] bottle for any other purpose than the bottling of COCA-COLA, and not in any territory except as herein referred to.

A typical license between respondents Coca-Cola Bottling Co. (Thomas), Inc. and Coca-Cola Bottling Works (Thomas), Inc. and the bottlers of each provides in part that licensor, wishing to assign to the bottler certain rights as to a specifically described geographic territory which has been received by approved transfer from The Coca-Cola Company, agrees:

> . . . to obtain and furnish to party of the second part [bottler] and only to obtain, for the territory herein referred to, sufficient syrup for bottling purposes to meet the requirements of party of the second part in the territory herein described, provided [6] party of the first [licensor] can obtain the delivery to it of such syrup from The Coca-Cola Company under the contract existing between party of the first part and The Coca-Cola Company.
>
> * * * * * * *
>
> [To select bottler] . . . as its sole and exclusive customer and licensee for the purpose of bottling Bottlers' Coca-Cola syrup, and using the name Coca-Cola thereon in the territory herein described.

In consideration therefor, bottler agrees:

> . . . Not to use the name Coca-Cola nor bottle nor vend said product except in the territory herein referred to without the written consent of party of the first part and The Coca-Cola Company. This limitation, however, is not to prevent party to the second part from obtaining such rights from parties authorized to use the name Coca-Cola and to bottle and vend said product.

* * * * * * *

> . . . To order, for the purpose of bottling Coca-Cola, the distinctive bottle, and none other, adopted or that may be adopted by party of the first part; to use said distinctive bottle and none other, in bottling Coca-Cola, and not to use said distinctive bottle for any other purpose than the bottling of Coca-Cola, and not in any territory except as herein referred to without the written consent of party to the first part and The Coca-Cola Company.

The license restrictions between Coca-Cola Bottling Works 3rd, Inc. and its bottlers are substantially similar to that of Coca-Cola, Coca-Cola Bottling Co. (Thomas), Inc. and Coca-Cola Bottling Works (Thomas) Inc. Coca-Cola is a party to the agreement between Coca-Cola Bottling Co. (Thomas), Inc., Coca-Cola Bottling Works (Thomas), Inc. and Coca-Cola Bottling Works 3rd, Inc. and their bottlers.

PAR. 7. The aforesaid agreements used by respondents have had, and may continue to have, the following effects:

(a) Competition between and among respondents' bottlers in the distribution and sale of "Coca-Cola" ("Coke"), "TAB," "Sprite," "Fresca," "Fanta" and "Simba" brands of soft drink products has been eliminated; [7]

(b) Competition between and among Coca-Cola's bottling operations and its bottlers in the distribution and sale of Coca-Cola soft drink products at the wholesale level has been eliminated;

(c) Competition between and among Coca-Cola's bottling operations and bottlers licensed by Coca-Cola Bottling Co. (Thomas), Inc., Coca-Cola Bottling Works (Thomas), Inc. and Coca-Cola Bottling Works 3rd, Inc. in the sale and distribution of Coca-Cola's soft drink products at the wholesale level has been eliminated;

(d) Competition between and among bottlers licensed by Coca-Cola and bottlers licensed by Coca-Cola Bottling Co. (Thomas), Inc., Coca-Cola Bottling Works (Thomas), Inc. and Coca-Cola Bottling Works 3rd, Inc. in the sale and distribution of Coca-Cola soft drink products at the wholesale level has been eliminated;

(e) Innumerable retailers and other customers have been deprived of the right to purchase "Coca-Cola" ("Coke"), "TAB," "Sprite," "Fresca," "Fanta" and "Simba" brands of soft drink products from the bottler of their choice at competitive prices; and

(f) Consumers of "Coca-Cola" ("Coke"), "TAB," "Sprite," "Fresca," "Fanta," and "Simba" brands of soft drink products have been deprived of the opportunity of obtaining such products in an unrestricted market and at competitive prices.

PAR. 8. Respondents' contracts, agreements, acts, practices and methods of competition aforesaid have had, and may continue to have, the effect of lessening competition in the advertising, merchandising, distribution, offering for sale and sale of pre-mix and post-mix syrups and soft drink products; deprive, and may continue to deprive, the public of the benefits of competition in the purchase of pre-mix, post-mix and soft drink products; and constitute unfair methods of competition and unfair acts or practices, in commerce, in violation of Section 5 of the Federal Trade Commission Act.

INITIAL DECISION BY JOSEPH P. DUFRESNE, ADMINISTRATIVE LAW JUDGE

OCTOBER 3, 1975

PRELIMINARY STATEMENT

In a complaint dated July 15, 1971, the Commission charged respondents with violation of Section 5 of the Federal Trade Commission Act (15 U.S.C. 45). The crux of the charges was that the territorial exclusivity provisions in trademark licensing contracts The Coca-Cola Company (hereinafter "Coca-Cola") enters with its bottlers impose an illegal restraint on competition. The provision limits the geographical territory in which a bottler may manufacture and sell "Coca-Cola" products.

It was alleged that the illegal effects of the provision were that competition had been eliminated:

(a) between independent bottlers of "Coca-Cola" products;

(b) at the wholesale level between independent bottlers of "Coca-Cola" products and "Coca-Cola's" own bottlers;

(c) at the wholesale level between "Coca-Cola's" own bottling operations and bottlers licensed by the other respondents; and

(d) at the wholesale level between bottlers licensed by "Coca-Cola" and those licensed by the other respondents.

It also was alleged that retailers and other customers had been deprived of the right to purchase "Coca-Cola" products from the bottler of their choice at competitive prices.

Lastly, it was alleged that consumers of "Coca-Cola" products have been deprived of the opportunity of obtaining "Coca-Cola" products in an unrestricted market and at competitive prices. [4]

In their answers, "Coca-Cola" and the three other respondents (Coca-Cola Bottling Co. (Thomas), Inc. (hereinafter Thomas Company), Coca-Cola Bottling Works (Thomas), Inc. (hereinafter Thomas Works), and Coca-Cola Bottling Works 3rd, Inc. (hereinafter Works 3rd)) admitted that they are "in commerce" within the meaning of the Federal Trade Commission Act. They denied that the territorial exclusivity provisions have any illegal anticompetitive effects.

As an affirmative defense, respondents stated that in *The Coca-Cola Bottling Co.* v. *The Coca-Cola Co.*, 269 F. 796 (D. Del. 1920), the District Court held in an opinion which has not been rescinded, vacated or modified, that the restraints included in the contracts between respondents and the bottlers are lawful and valid under federal and state antitrust laws and not in unreasonable restraint of trade.

They also asserted the defense that the Commission had failed to include indispensable parties, the bottlers, who were the other parties to the contracts, and that to the extent the Commission's proceeding sought to eliminate or abridge the respondents' and bottlers' contractual property rights, the proceeding would impose a penalty or forfeiture barred by the statute of limitations (28 U.S.C. 2462).

Lastly, in summary, they asserted (1) that a Commission order would place them in the position of violating either that order or the District Court's order, depending on which they complied with; (2) that the effect of a Commission order would be unfair to consumers and small businessmen bottlers and anticompetitive by increasing prices and accelerating the demise of small grocers; (3) that respondents' constitutional right to due process would be violated; and (4) that there is no public interest in the proceeding.

Because of the time which has elapsed since the complaint issued, it is appropriate to set forth a listing of significant events which have taken place in this proceeding since July 15, 1971. These were: [5]

1. On July 30, 1971, a Motion for Consolidation of this case with Dkts. 8853–8859, which pertain to exclusive territory provisions in the bottler licensing contracts used for other national brands of soft drinks, was filed by complaint counsel. That Motion was denied by the administrative law judge on September 28, 1971.

2. On August 27, 1971, September 8, 1971, and December 14, 1971, motions to dismiss the complaint for non-joinder of indispensable parties (*i.e.*, all of the licensee bottlers) were filed by "Coca-Cola," the other respondents, and the intervenors participating in the proceedings at that time. These motions were denied by the administrative law judge on January 7 and 12, 1972.

3. On April 21, 1972, the respondents filed a complaint for injunctive relief and a declaratory judgment against the Commission

in the United States District Court for the Northern District of Georgia. The Court dismissed the complaint on May 22, 1972. That dismissal was appealed to the United States Court of Appeals for the Fifth Circuit on June 6, 1972. The appellate court affirmed the decision of the District Court on February 20, 1973. On May 8, 1973, respondents sought *certiorari* to the Supreme Court; however, the Court denied the writ on October 9, 1973 (*Coca-Cola Co.* v. *Federal Trade Commission*, 342 F. Supp. 670 (N.D. Ga. 1972), *aff'd*, 475 F.2d 299 (5th Cir. 1973), *cert. denied*, 414 U.S. 877 (1973)).

4. On July 31, 1972, former complaint counsel filed a motion for partial summary decision. That motion was denied by the administrative law judge on April 5, 1973.

5. On March 15, 1974, intervenors Association, Scioto, Elberton, Roddy, Westminster, and Texas filed a motion to require complaint counsel to file an environmental impact statement and to stay the proceedings until such a statement is filed. The administrative law judge denied that motion on April 2, 1974. The intervenors then filed a motion to reconsider or to certify the motion to the Commission on April 10, 1974. That motion was denied by the administrative law judge on May 30, 1974. [6]

6. On July 30, 1974, complaint counsel filed a motion to authorize disclosure of documents containing nonpublic business information to be used at the hearings. On October 3, 1974, the administrative law judge authorized the disclosure.

7. On August 12, 1974, respondents and intervenors filed a motion for issuance of a subpoena duces tecum to the Secretary of the Commission to have him produce materials in the Commission's nonpublic files. Briefs in support and opposition were filed on December 9 and 10, 1974. The subpoena was quashed by order of the Commission dated March 4, 1975.

It also should be pointed out that in addition to the intervenors identified above a number of petitions to intervene were filed by a variety of other, small and large Coca-Cola bottlers beginning on September 3, 1971, with the last filed on March 11, 1975. All such petitions were granted. As a result, there were 14 individual bottler intervenors plus the Coca-Cola Bottlers' Association. In early 1971, 99 percent of the domestic bottlers of Coca-Cola, accounting for about 815 productive facilities, were members of the Association.

The adjudicative hearings were held in Washington, D.C., from May 5 through June 11, 1975. The record was closed for the reception of evidence on July 7, 1975.

The findings of fact following are based on a review of the allegations made in the complaint, respondents' answers, stipulations entered by counsel, the evidentiary record and upon a reading of the transcript record of the testimony and consideration of the demeanor of the witnesses at the hearings. In addition, the proposed findings of fact, conclusions and orders, together with reasons and briefs in support thereof filed by both sides have been given careful consideration. To the extent not adopted by this decision in the form proposed or in substance, they are rejected as not supported by the record or as immaterial. [7]

For the convenience of the Commission and other readers of this initial decision, the findings of fact include references to supporting evidentiary items in the record. Such references are intended to serve as guides to the testimony, evidence and exhibits supporting the findings of fact. They do not necessarily represent complete summaries of the evidence considered in arriving at such findings. The following abbreviations have been used:

CX – Commission's Exhibit, followed by number of exhibit being referenced.

RX – Respondents' Exhibit, followed by number of exhibit being referenced.

Tr. – Transcript preceded by the name of the witness and followed by the page number.

FINDINGS OF FACT

The Coca-Cola Company

1. In 1886 Mr. John S. Pemberton invented a formula for a soft drink syrup and first prepared and sold a soft drink made pursuant to that formula under the trademark Coca-Cola (Stipulation No. 1, RX 1A, Tr. 555; Smith Tr. 677).

2. In 1891 Mr. Asa G. Candler acquired Mr. Pemberton's rights to the secret formula for Coca-Cola and to the trademark Coca-Cola. In 1892 Mr. Candler formed The Coca-Cola Company, a Georgia corporation, predecessor in interest to the respondent "Coca-Cola" (Smith, Tr. 678; Stipulation No. 1, RX 1A–B, Tr. 555). [8]

3. Respondent, "Coca-Cola," is a corporation organized, existing and conducting its business under and pursuant to the laws of the State of Delaware. "Coca-Cola" maintains an office and its principal place of business at 310 North Ave., NW., Atlanta, Georgia. "Coca-Cola" and its subsidiaries in 1968 had consolidated net sales of $1,185,808,864 and consolidated assets of $802,100,548. Approximately one-third and more of the sales are accountable to foreign operations. In 1968 "Coca-Cola" sold or shipped syrup or concentrates to

approximately 900 domestic bottlers located throughout the United States. (Admitted in Answer; Stipulation No. 2, CX 1243A–B, Tr. 465.) When the complaint issued in July 1971, there were 726 bottlers operating 804 bottling plants (Smith, Tr. 687).

Respondents' Business

4. "Coca-Cola," through its Coca-Cola U.S.A. division, is engaged principally in the manufacture and sale of syrup (a mixture of ingredients in liquid form which, when properly mixed with pure carbonated water, becomes the finished soft drink product (Smith, Tr. 569)) and concentrates (a mixture of basic ingredients to which sugar must be added by the bottler to prepare a syrup (Smith, Tr. 570)). The syrup and concentrate are used in the processing and sale of soft drinks under one or more of the trade names Coca-Cola or Coke, TAB, Sprite, Fresca, Fanta, Simba, Santiba, and Mr. PiBB. (Admitted in Answer; Smith, Tr. 584–586.)

5. Coca-Cola is a cola type drink. TAB is a low calorie cola drink. Fresca is a citrus base, low calorie drink. Sprite is a lemon-lime drink. Fanta is a trademark which is applied to a line of flavored drinks including orange, root beer, gingerale, and strawberry. Simba is no longer on the market. Santiba is a trademark which is applied to a line of mixers such as carbonated water, gingerale and Tom Collins mix. Mr. PiBB, a relatively new product, is a pepper type drink. Products other than Coca-Cola are referred to as "allied products" (Smith, Tr. 584–586). [9]

6. Beginning in 1955, "Coca-Cola" from time to time authorized its licensed bottlers to bottle and sell Coca-Cola and allied products (as they were introduced) in an increasingly wide variety of sizes and types of containers. Coca-Cola and allied products currently are offered in returnable bottles, non-returnable bottles, and cans. Package sizes include 6 1/2-ounce, 10-ounce, 12-ounce, 16-ounce, 32-ounce, 48-ounce, and 64-ounce containers. It is being test marketed in a 72-ounce size (Smith, Tr. 714).

7. "Coca-Cola's" Foods Division manufactures other beverage products, including Maryland Club coffee, Hi-C fruit drinks, Minute Maid orange juice, Snow Crop orange juice, and other citrus products (Smith, Tr. 573, 580). Its Temco subsidiary produces private label spray and freeze dried instant coffee (Smith, Tr. 573) and its Aqua-Chem, Inc., subsidiary manufactures steam boilers and water purification equipment (Smith, Tr. 573).

8. In July 1971, "Coca-Cola" had 8 subsidiaries which operated 27 bottling plants in various cities of the United States and sold soft drink products to retailers in the areas thereof (Smith, Tr. 687–688).

9. The bottler subsidiaries of "Coca-Cola" today are:

The Coca-Cola Company of New England (Dedham, Mass.);
The Coca-Cola Bottling Company of Baltimore (Maryland);
The Coca-Cola Bottling Company of Ohio (Columbus, Ohio);
The Coca-Cola Bottling Company of Michigan (Lansing, Mich.);
The Coca-Cola Bottling Company of Wisconsin (Milwaukee, Wis.);
The Coca-Cola Bottling Company of Chicago (Illinois);
The Coca-Cola Bottling Company of California (San Francisco); and
The Pacific Coca-Cola Bottling Company (Bellevue, Wash.).

In 1971, these companies served areas containing approximately 14 percent of the population of the United States (Ogden, Tr. 828, 844). [10]

10. Most of the subsidiary bottling plants were acquired years ago to assure the availability of Coca-Cola in territories when bottlers in those territories had to sell out or did not have the financial resources and independent firms with money and know-how were unavailable in those areas (Susong, Tr. 913, 922). The policy of the company for over a decade has been that such a subsidiary bottler is to be sold when the company acquires one so that the number of subsidiaries remains stable (Susong, Tr. 914, 921).

11. Another subsidiary, Canners of Coca-Cola Bottlers, Inc. (hereinafter Canners), constructed canning plants in the 1960's to provide Coca-Cola and allied products in cans to bottlers under agency agreements in areas where there was inadequate canning capacity (Ogden, Tr. 825, 837).

12. Canners' plants are located at Nashua, New Hampshire; Baltimore, Maryland; College Park, Georgia; Columbus, Ohio; Alsip, Illinois; and San Leandro, California (Ogden, Tr. 824). As independent bottlers in some areas desire to invest in them, the company has sold canning plants, *e.g.*, in Salt Lake City, Utah; Plymouth, Florida; Greensboro, North Carolina; Houston, Texas; and Phoenix, Arizona (Ogden, Tr. 825–826).

13. Total dollar sales of soft drink syrup by "Coca-Cola" to bottlers in the United States for the indicated years were as follows:

1964	$173,961,477
1965	184,959,054
1966	211,629,426
1967	227,844,768
1968	246,962,024

(CX 4F). [11]

14. Total dollar sales and total assets of "Coca-Cola" for the indicated years were as follows:

	Sales	Assets
1968	$1,185,808,864	802,100,548
1969	1,365,443,068	802,100,548
1970	1,606,401,160	1,005,777,214
1971	1,728,827,572	1,107,873,472
1972	1,876,192,397	1,231,612,887

(CX 51 – CX 54).

15. In July of 1971, "Coca-Cola" produced its full line of soft drink syrups and concentrates in plants at the following locations which supplied all of the licensed Coca-Cola and allied product bottlers in the United States:

Atlanta, Georgia
Baltimore, Maryland
Chicago, Illinois
Columbus, Ohio
Dallas, Texas
Ewa Beach, Hawaii
Houston, Texas
Kearny, New Jersey
Los Angeles, California
Nashua, New Hampshire
New Orleans, Louisiana
Plymouth, Florida
Portland, Oregon
St. Louis, Missouri
San Francisco, California

(Ogden, Tr. 811–815). [12]

The Other Respondents

16. In 1899 "Coca-Cola" granted to Mr. B. F. Thomas and Mr. Joseph B. Whitehead the exclusive right to bottle Coca-Cola and to sell Coca-Cola in bottles throughout the United States with the exception of the six New England States and the States of Mississippi and Texas where local jobbers were already bottling Coca-Cola on a very small scale, with the permission of "Coca-Cola" but without a contractual agreement. The sale of fountain syrup was specifically reserved to

"Coca-Cola" (Smith, Tr. 679–680; Stipulation No. 1, RX 1B, Tr. 555; CX 4A).

17. Lacking sufficient capital or time to build sufficient plants expeditiously to bottle Coca-Cola and to create consumer demand throughout the area covered in the 1899 contract with "Coca-Cola," Messrs. Thomas and Whitehead divided their territory between them. Mr. Thomas' interest was termed *The* Coca-Cola Bottling Company (Stipulation No. 1, RX 1C, Tr. 555).

18. The Coca-Cola Bottling Company was soon succeeded in interest by Coca-Cola Bottling Co. (Thomas), Inc. Coca-Cola Bottling Co. (Thomas), Inc., transferred part of its territory to a sister company, Coca-Cola Bottling Works (Thomas), Inc. It also licensed Coca-Cola Bottling Works 3rd, Inc., to act as licensor with respect to certain designated territory (CX 4B; Tr. 488).

19. *The* Coca-Cola Bottling Company, under Mr. Whitehead and his new partner John T. Lupton, also formed several Parent Bottling Companies to whom the right to act as licensor with respect to certain territory was conveyed (CX 4B, Tr. 488). [13]

20. Beginning in 1900, Coca-Cola Bottling Company (Thomas) and *The* Coca-Cola Bottling Company (Whitehead) initiated a program aimed at granting exclusive licenses to local bottling companies throughout their respective territories. By 1920, they and the Parent Companies which they had formed had licensed over 880 local bottling companies to produce and sell Coca-Cola in bottles (Smith, Tr. 680; Stipulation No. 1, RX 1D, Tr. 555).

21. Respondent Thomas Company is a corporation organized, existing and conducting its business under and pursuant to the laws of The State of Delaware. It maintains its office and principal place of business at 1600 American Bank Building, Chattanooga, Tennessee 37402. In 1968, Thomas Company made sales to 122 bottlers located principally in Alabama, Delaware, Indiana, Maryland, Mississippi, New Jersey, New York, North Carolina, Ohio, Pennsylvania, Virginia, and West Virginia. These bottlers had contracts with 45 sub-bottlers in Illinois, Maryland, Mississippi, Missouri, New Jersey, New York, Ohio, Pennsylvania, Virginia, and West Virginia (Stipulation No. 2, CX 1243B, Tr. 465, 467; Susong, Tr. 491).

22. Respondent Thomas Works is a corporation organized, existing and conducting its business under and pursuant to the laws of the State of Delaware. It maintains its office and principal place of business at 1600 American Bank Building, Chattanooga, Tennessee. In 1968, Thomas Works made sales to 38 bottlers located principally in Alabama, Georgia, Kentucky, and Tennessee. These bottlers had

contracts with 13 sub-bottlers in Alabama and Kentucky (Stipulation No. 2, CX 1243B–C, Tr. 466, 467; Susong, Tr. 491). [14]

23. Respondent Works 3rd is a corporation organized, existing and conducting its business under and pursuant to the laws of the State of Delaware. It maintains its office and principal place of business at 1600 American Bank Building, Chattanooga, Tennessee. In 1968, Works 3rd made sales to five bottlers located principally in Pennsylvania and New Jersey. (Admitted in Answer; Stipulation No. 2, CX 1243C, Tr. 466.)

24. Thomas Company and Thomas Works contract with bottlers pursuant to agreement with "Coca-Cola" under which the bottlers bottle and sell Coca-Cola soft drinks in their territories. Works 3rd contracts with Thomas Company for the same purpose. These three respondents engage principally in the purchase of Coca-Cola syrups for sale to numerous bottlers they have licensed in the various States of the United States. (Admitted in Answer; Stipulation No. 2, CX 1243D–E, Tr. 465–467.)

25. Since 1923, "Coca-Cola" has acquired all of the original Parent Bottling Companies with the exception of the three Thomas Companies. In doing so, "Coca-Cola" has acquired all of their rights and assumed all of their obligations. "Coca-Cola" presently deals directly with those bottlers not under contract to the three Thomas Companies in connection with bottled Coca-Cola and deals directly with all bottlers, including the Thomas bottlers, in connection with the bottling of all allied products (Susong, Tr. 538).

Interstate Commerce

26. Each of the respondents is engaged in "commerce" within the meaning of the Federal Trade Commission Act (15 U.S.C. 44). (Admitted in Answer.) There is a regular and continuous flow in interstate commerce of syrups and concentrates produced by "Coca-Cola," between syrup and concentrate manufacturing facilities located in various states, and production facilities of "Coca-Cola" located in other states (Ogden, Tr. 812–17). [15]

History of the Soft Drink Industry

27. The bottling of flavored carbonated soft drinks did not begin in the United States on a significant scale until the latter half of the nineteenth century. Prior to 1850 such soft drinks had been served almost exclusively at soda fountains for immediate consumption. During the late 1800's a growing number of extract or syrup manufacturers entered the business. These persons and companies developed and introduced many new proprietary flavors, including

Hires, Vernor's, Clicquot Club, Dr Pepper, Coca-Cola, and Pepsi-Cola (Stipulation No. 3, CX 1244A, Tr. 470).

28. Around the turn of the twentieth century syrup companies were largely small operations, typically owned by pharmacists or their families (Stipulation No. 3, Tr. 471). In order to provide the necessary inducement for local entrepreneurs to supply the capital required and to make the necessary effort to promote consumer acceptance of new bottled soft drink products, soft drink licensors included exclusive territorial provisions in trademark licenses (Stip. No. 3, CX 1244B–C, Tr. 471–72).

29. Territorial restrictions encouraged greater development of marketing and distribution efforts since exclusive licensees knew that their licensors and other licensees could not obtain a "free ride" on their efforts; they made possible the licensor's maintenance of quality control, thereby insuring uniform application of his common law trademark; they facilitated the licensor's production planning by enabling greater accuracy in calculating the forthcoming demand for syrup in a territory; they reduced the selling cost of the product by avoiding duplication of sales effort in a territory; and they encouraged the bottler to develop the potential of his territory to the fullest, thereby maximizing sales of the trademarked product (Stip. No. 3, CX 1244C, Tr. 471–72). **[16]**

30. The system of exclusive territorial licenses consistently has been widely employed in the manufacture and distribution of bottled soft drinks. There are over 50 syrup companies who have licensed local bottlers, 36 of them nationwide. These companies market more than 150 different soft drink brands through 7,500 agreements with local bottlers. These agreements for the local production and sale of trademarked products are unique when compared with the traditional organizational structure of American manufacturing and marketing (Stip. No. 3, CX 1244D, Tr. 472–73).

31. One unique feature of the soft drink trademark licensing system is that a nationally advertised product is manufactured locally by independent businessmen who are required to make substantial and continuing investments in plant, equipment, packaging and warehouse space (Clements, Tr. 4029–31). No other industry could be identified where a single national brand owner sells an ingredient to hundreds of independent licensees who manufacture a finished product from that ingredient and others under a trademark license (Clements, Tr. 4032).

32. The soft drink industry is also unique in that it sells a refreshment product which is an "impulse item" (Clement, Tr. 4029), whose most important characteristic is a distinct taste (Clements, Tr. 2989–90, 4032). Constant sampling is necessary to maintain demand for

a brand (Clements, Tr. 4033), and total availability of a brand at a multiplicity of outlets is essential to provide constant sampling necessary to successful marketing of that brand (Clements, Tr. 4029; Reid, Tr. 3554). The soft drink industry is also different from other industries in the broad range of flavors and package sizes and types required to be made available to satisfy consumer demand (Millard, Tr. 2319–20, 2321), in the need for frequent local store-door service (Millard, Tr. 2319, 2324–25), the importance of in-store merchandising (Millard, Tr. 2324–25), and the requirement of a store-door delivery system to sustain the use of a returnable container (Clements, Tr. 4029–30). Soft drinks are the only major product still available in food stores in returnable containers (Ellis, Tr. 944–45, 1022). [17]

33. The syrup company manufactures and sells syrup or flavoring concentrates to the bottlers. Syrup companies also participate in many of the advertising and promotion programs made in connection with their trademarked products, provide advice and technical assistance on production, quality control, management and sales problems, and engage in development and test marketing of new products and containers (Stip. No. 3, CX 1244D, Tr. 473).

34. The bottlers are the manufacturers and distributors of trademarked soft drinks produced from the licensor's syrup or concentrate and manufactured according to his quality standards and specifications. The bottler decides on the plant and equipment to be used, the volume of production by size and type of container and product mix, as well as the price to be charged and the manner in which he can maximize his market penetration and secure the widest possible distribution of trademarked soft drinks throughout his territory (Stip. No. 3, CX 1244E, Tr. 473–74).

35. In most local markets, there are independent producers who manufacture and sell soft drinks under their own labels. Generally, these local and regional brands are not franchised. In recent years, however, several of these companies have expanded from their local bases and have begun to compete in regional and national markets. For example, Shasta, which just over 10 years ago was marketed exclusively on the West Coast, is now available in all states. Frank's is currently marketed in many areas on the East Coast, and Faygo has branched out into almost a dozen eastern and midwestern states. In the process of expansion, these and other local and regional brands have utilized various techniques—distant shipments from existing plants, the establishment of new production facilities in other parts of the country, contract producers and in a few cases, territorial license agreements (Stip. No. 3, CX 144E–F, Tr. 474). [18]

36. Since the early 1960's, private label soft drink brands have

become a substantial competitive force in the soft drink industry. These are sold by a retailer under the retailer's own trade name or under a trade name of a wholesaling or other organization from which the retailer purchases, *e.g.*, 7-Eleven, Yukon Club (A&P), and Gayla (Topco). Private label soft drinks are manufactured either by the retailers or wholesalers themselves or for them by contract bottlers or canners and are generally sold for home consumption in non-returnable bottles and cans. Hundreds of new private labels have entered the market, many in the last five years. In the Washington, D.C., metropolitan area for example, over 15 private label brands are being marketed. Retailers are able to allocate scarce shelf space and prime store locations to their own private label soft drinks and are able to promote them vigorously with both point-of-sale and local media advertising (Stip. No. 3, CX 1244F, Tr. 474–75).

37. Flavored carbonated soft drinks are only one of a number of other commercial beverages available to the American consumer. Coffee is and has been America's most popular commercial beverage. In 1950, soft drinks represented an estimated 10 percent of the total commercial beverage market; by 1970, soft drinks had more than doubled their market share, accounting for an estimated 21 percent. Soft drink consumption has been climbing rapidly, growing at an annual rate of approximately 6 percent for the last 2 decades. This increase enabled flavored carbonated soft drinks to become the nation's second most popular commercial beverage in 1969. Such soft drinks may in the near future overtake coffee as America's number one commercial beverage (Stip. No. 3, CX 1244F–G, Tr. 475–76).

38. Soft drink consumption patterns exhibit both a high degree of regional and seasonal variation. Consumption of soft drinks is higher in summer months and in areas with warm and humid climates, such as the South (Stip. No. 3, CX 1244G, Tr. 476). [19]

39. Consumer taste, flavor preferences, and willingness to try new products also have an impact on soft drink consumption patterns. On a national basis, cola has been the most popular soft drink flavor since 1920 when it surpassed gingerale. Since 1947, various studies have shown that the cola flavor accounts for approximately 60–65 percent of all soft drinks sold. While the share accounted for by cola drinks may have dipped slightly in recent years, according to some surveys, cola is America's most popular flavor, followed by lemon-lime, orange, gingerale, and root beer. As with soft drink consumption, flavor preferences exhibit wide regional variation, with cola more popular in the South than in other areas of the country (Stip. No. 3, CX 1244G–H, Tr. 476).

40. The emergence of low-calorie soft drinks in the last 20 years

also has been responsible for creating a number of new soft drink consumers. Before the introduction of low-calorie soft drinks, consumers voiced two primary reasons for avoiding soft drinks—caloric content and restricted diet. With the advent of the dietetic drinks, these two barriers were overcome. Although "No-Cal" and "Diet-Rite" were originally marketed in 1953, diet-flavored soft drinks did not become a significant market factor until the early 1960's. Following the cyclamate ban in October 1969, which virtually removed low-calorie soft drinks from the market, soft drink companies marketed saccharin substitutes, which by the end of 1970 had recaptured about 10 percent of total soft drink sales (Stip. No. 3, CX 1244H–I, Tr. 477).

41. The last 10 years have also seen the introduction of a variety of completely new soft drink categories including "isotonic" and "thirst-quenching" soft drinks, such as "Gatorade." Since 1960, a score of new trade names and flavors also have been introduced. The increase in per capita soft drink consumption has thus in part been brought about by the ability of the soft drink industry to develop new soft drink products, brands and flavors, and the willingness of the consumer to accept them (Stip. No. 3, CX 1244I, Tr. 477–78). [20]

42. Other factors contributing to the growth in per capita consumption of soft drinks are the general increase in disposable personal income and the increasing tendency of Americans to congregate in urban areas. Two other contributions to the growth in per capita soft drink consumption have been the major shift from small size (6–8 oz.) over to medium size containers (10–16 oz.), particularly in the home market, but also in vending machines dispensing packaged products, and the ability of the industry to make readily available at virtually every location soft drinks in a wide variety of brands, flavors, and packages (Stip. No. 3, CX 1244I, Tr. 478).

43. In 1971, soft drinks were available in more than 99 percent of the over 200,000 retail food outlets in the United States. In addition, soft drinks are available in virtually every service station, restaurant, sports stadium, and theater in the country. The total number of retail outlets dispensing or selling soft drinks is well over a million (Stip. No. 3, CX 1244J, Tr. 478–79).

44. In recent years, there has also been a rapid proliferation of vending machines, which has produced an even more intensive coverage of the market. In 1971, there were nearly 1,400,000 vending machines dispensing soft drinks in bottles, cans, and cups (Stip. No. 3, CX 1244J, Tr. 479).

45. Fountain-dispensed soft drinks are available in well over 100,000 retail outlets. The rapid expansion of drive-in eating and

drinking places in recent years has also spurred fountain sales of soft drinks (Stip. No. 3, CX 1244J, Tr. 479).

46. The wide availability of flavored carbonated soft drinks is in part attributable to the high degree of market penetration achieved by bottlers of national brands employing store-door delivery in well-defined areas (Stip. No. 3, CX 1244J, Tr. 479). [21]

47. In addition to increased availability of soft drinks generally, there has been a proliferation of brands, flavors, and containers for the consumer to select from. At a given outlet, it is not uncommon for the consumer to have a choice of 25–30 flavors, both in dietetic and regular form (Stip. No. 3, CX 1244J–K, Tr. 479).

48. Since the turn of the century, soft drink consumption has undergone significant changes. In 1900, 70 percent of soft drinks were consumed on the premises of the vendors, and 30 percent were consumed in homes. Most of the flavored carbonated soft drinks consumed on the premises were dispensed from soda fountains; soft drinks consumed at home were for the most part delivered direct from the bottling plant. With the emergence of supermarkets in the 1930's, the development of the six-bottle carton "Home Package" for Coca-Cola in 1922, the distribution of Coca-Cola in coin-operated vending machines in 1935, the patterns of soft drink distribution and consumption began to change. By the mid-twentieth century, the modern self-service supermarket had become a widespread reality. In the mid-1950's, soft drinks sold for home consumption first surpassed those sold for consumption on the premises. Nationally, food stores account for between 85 percent to 90 percent of the sales for home consumption, or just above 50 percent of total soft drink sales. Soft drinks purchased for home consumption are typically purchased in medium-to-large-size containers (10 oz. and above) and multi-container cartons (Stip. No. 3, CX 1244K–L, Tr. 480).

49. With regard to consumption on the premises, the market is relatively evenly divided between vending machines (which account for approximately 18 percent of total flavored carbonated soft drink sales) and service sales at counters and tables (also approximately 18 percent). Canned and bottled soft drinks compete with bulk soft drinks dispensed at soda fountains and in cup vending machines (Stip. No. 3, CX 1244L, Tr. 480). [22]

50. In the United States, production and consumption of flavored, carbonated soft drinks have increased dramatically over the years, as evidenced by the following table:

Year	Total Value $ (Wholesale)	Total Cases (192 ounce)	Per Capita (8 oz. containers)
1849	760,000	1,520,000	1.6
1859	1,415,000	2,830,000	2.2

1869	4,222,000	8,444,000	6.4
1879	4,742,000	9,484,000	4.5
1889	14,354,000	26,098,180	9.9
1899	23,269,000	38,781,660	12.2
1909	43,508,000	62,154,280	16.2
1919	135,341,000	169,176,200	38.4
1929	214,322,238	272,428,486	53.1
1939	361,690,917	482,995,676	88.6
1940	411,699,200	550,400,000	100.1
1941	553,879,040	740,480,000	133.6
1942	526,185,088	703,456,000	126.2
1943	580,351,000	773,801,600	138.6
1944	629,681,100	812,491,700	147.1
1945	584,994,000	731,242,500	132.9
1946	617,168,600	771,460,800	132.3
1947	745,676,000	901,664,000	150.9
1948	835,157,300	1,009,863,700	164.4
1949	860,959,300	1,012,893,300	162.0
1950	876,532,600	1,001,751,474	158.0
1951	939,442,500	1,043,825,000	162.7
1952	1,019,295,000	1,132,550,000	174.0
1953	1,089,513,000	1,177,852,000	177.5
1954	1,166,605,000	1,176,674,000	174.2
1955	1,252,276,000	1,264,925,000	184.2
1956	1,308,000,000	1,321,214,000	188.9

1957	1,347,241,500	1,360,850,000	189.2
1958	1,427,463,500	1,359,489,000	186.4
1959	1,633,015,900	1,484,560,000	199.8
1960	1,698,025,600	1,476,544,000	192.0
1961	1,829,083,200	1,524,236,000	198.3
1962	2,001,016,800	1,667,514,000	213.4
1963	2,341,189,000	1,800,915,000	227.4
1964	2,533,167,000	1,948,590,000	242.9
1965	2,735,567,000	2,104,282,000	259.1
1966	3,175,980,000	2,352,587,000	287.0
1967	3,458,632,000	2,470,452,000	298.1
1968	4,165,552,000	2,777,035,000	331.6 [23]
1969	4,369,664,000	2,913,110,000	344.4
1970	4,799,784,000	3,096,635,000	362.8
1971	5,346,960,000	3,353,615,000	388.1
1972	5,683,820,000	3,541,417,000	406.4
1973	6,223,156,500	3,771,610,000	429.6

(CX 1261)

Bottlers and How They Operate

51. (Note: Complaint counsel called all of the Coca-Cola bottlers (17) in a "corridor" consisting generally of the area from southern Virginia to upstate New York. In addition, counsel for respondents called bottler witnesses, both for Coca-Cola and other brands whose territories are located in widely separated parts of the United States. These bottler witnesses typify all licensed bottlers in that they cover the spectrum of firms classifiable as urban, suburban, rural, single plant, multi-plant, large, small, first line bottlers, sub-bottler, marketing bottler (*i.e.*, one with no production facilities), multi-territory,

single territory, privately held, publicly held, "Coca-Cola" subsidiary, etc.)

52. Most bottlers of Coca-Cola are small, independent manufacturers. Their size can be measured by (1) the population in a bottler's territory (Wimberly, Tr. 871–72), (2) the bottler's annual case sales of soft drinks (Wimberly, Tr. 872; Susong, Tr. 920; Sales, Tr. 1285), or (3) the number of bottler's employees (RX 36 (p. 2)).

53. Bottlers of Coca-Cola whose territories contain less than 250,000 people include Hartwell, Georgia (35,000 (Rooks, Tr. 1360)); Spirit Lake, Iowa (175,000 (LaDoux, Tr. 1458)); Montross, Virginia (39,000 (Carver, Tr. 1619)); Jamestown, North Dakota (112,000 (Bernabucci, Tr. 1956)); Coatsville, Pennsylvania (240,000 (Filoromo, Tr. 2168)); Dover, Delaware (85,000 (Massey, Tr. 2236)); Westminster, Maryland (128,000 (Roadcap, Tr. 2432–33)); and Ada, Oklahoma (82,000 (Crabtree, Tr. 2662)). Territories between 250,000 and 500,000 people [24] include LaCrosse, Wisconsin (300,000 (Bernabucci, Tr. 1965)); Washington, Pennsylvania (380,000 (Cameron, Tr. 2043–44)); and Stockton, California (290,000 (DeLap, Tr. 2564)). Territories between 500,000 and 1,000,000 people include The Coca-Cola Bottling Company of the Peninsula in Belmont, California (700,000 (Sheldon, Tr. 2607)).

54. In 1974, there were 111 independently owned bottlers of Coca-Cola which had sales below 250,000 equivalent cases of 24 eight ounce bottles; 98 independently owned bottlers of Coca-Cola which had equivalent case sales between 250,000 and 500,000; 87 which had case sales between 500,000 and 1,000,000; and 47 which had between 1,000,000 and 2,000,000 cases (Susong, Tr. 914–15). Of these 343 bottlers with sales below two million cases, there was no common ownership or control (Susong, Tr. 915).

55. The Small Business Administration classifies any manufacturing business with less than 250 employees as a small business (RX 36 (p. 2)). The bottler system for "Coca-Cola" has a large number of small plants, with 85 percent having less than 100 employees (RX 35D). In the census of bottlers of Coca-Cola completed in 1974, of the 567 bottlers who responded, representing about 75 percent of all domestic bottlers of Coca-Cola (RX 35B), 193 had less than 25 employees, 168 had between 25 and 49 employees, 121 had 50–99 employees, 46 had 100–199 employees, and only 39 had more than 200 employees (RX 35P–35Y). Of these plants, 14 were owned by subsidiaries of "Coca-Cola." One of the 14 had less than 50 employees; one had between 50 and 100; five had between 101 and 200; and seven had over 200 (Bernabucci, Tr. 1954).

56. Bottlers are often closely held, family corporations (Brown, Tr. 1653; Burks, Tr. 3000; Ippolito, Tr. 3227). It is not unusual to find all

members of the family, including wives, grandparents, children and other relatives working in some capacity in the business. For example, the president of the Northern Neck Coca-Cola Bottling Company, Montross, Virginia, testified that his son is vice-president of the company and his daughter is secretary (Carver, Tr. 1590). The president of the Coatesville Coca-Cola Bottling Works, Coatesville, Pennsylvania, testified that his three brothers [25] work as sales manager, delivery driver and service manager, respectively, and that one of his sons is planning to go into the business, joining two nephews who are already full-time employees (Filoromo, Tr. 2167). The president of the Dr Pepper bottler in Galveston, Texas, testified that his wife is the company bookkeeper; his son is sales manager and truck checker; and his brother-in-law works in the company's office (Ippolito, Tr. 3229).

57. The bottler of Coca-Cola in Jamestown, North Dakota, testified that his father bought the company in 1933 when it was bankrupt (Bernabucci, Tr. 1955–56). In the Coatesville, Pennsylvania Coca-Cola Bottling Works, the first dividends were not paid until 1935. The founder's salary was so meager that he operated a grocery store with his wife and seven children because, as his son testified, "We had quite a task just keeping bread and butter on the table" (Filoromo, Tr. 2160). Bottlers of Coca-Cola and other national brands initially had to develop the demand for their respective products by sneaking bottles of their products into cases of more accepted "rainbow" flavors (Stokes, Tr. 1072; Cameron, Tr. 2034; Ippolito, Tr. 3228).

58. Bottlers build demand for Coca-Cola and other national brands by generating good will in the community, and have become identified with their products in their communities. For example, the bottler of Coca-Cola in Hartwell, Georgia, has his route salesmen operate a check cashing service for small stores located in rural areas (Rooks, Tr. 1373A).

59. Not all bottlers are small, family-owned corporations. Coca-Cola New York, a publicly held corporation, operates one of the largest independent soft drink businesses in the world with net sales in 1971 of $160,642,000. Coca-Cola New York operates 900 route delivery trucks, serves 70,000 accounts and almost 25 million people in New York, New Jersey, Pennsylvania, Connecticut, and Massachusetts. In addition to its soft drink operations, Coca-Cola New York has three subsidiary corporations: Mogen David Wine Corporation; Franzia Wine Company; and Igloo Corporation (Millard, Tr. 2248, 2318, 2323; CX 1220). [26]

60. The "Coca-Cola" and Thomas Companies licensing agreements have always and do now grant to the licensee the exclusive right to manufacture, distribute and sell trademarked soft drink products in

bottles and cans in a defined geographical area. The contracts limit the licensee to the sale of his products only for ultimate resale within the licensee's exclusive territory (Susong, Tr. 520; Smith, Tr. 588, 642).

61. License agreements in effect between "Coca-Cola" and its bottlers contain, and have contained the following typical provisions:

> . . . company agrees to furnish to bottler, and only to furnish to the territory herein referred to, sufficient syrup for bottling purposes to meet the requirement of the bottler in the territory herein described.
>
> * * * * * * *
>
> . . . company does hereby select bottler as its sole and exclusive customer and licensee for the purpose of bottling the bottler's bottle syrup, Coca-Cola, in the territory described.
>
> * * * * * * *
>
> [Bottler agrees] . . . not to use the trademarks Coca-Cola or Coke, nor bottle nor vend said product except in the territory herein referred to. This limitation, however, is not to prevent bottler from acquiring similar rights for other territory.
>
> * * * * * * *
>
> [Bottler agrees] . . . not to use said distinctive bottle for any other purpose than the bottling of Coca-Cola and not in any territory except as herein referred to.

(Susong, Tr. 506–508; CXs 10, 34, 40, 44–46, 48.) [27]

62. There are other similar agreements in effect between the Thomas Companies and their bottlers. All such Thomas bottler agreements contain, and have contained, the following typical provisions:

> [Licensor agrees] . . . to obtain and furnish to party of the second part [bottler] and only to obtain, for the territory herein referred to, sufficient syrup for bottling purposes to meet the requirements of the party of the second part in the territory herein described, provided party of the first part [licensor] can obtain the delivery to it of such syrup from The Coca-Cola Company under the contract existing between party of the first part and The Coca-Cola Company.
>
> * * * * * * *
>
> [Licensor agrees to select bottler] . . . as its sole and exclusive customer and licensee for the purpose of bottling Bottlers' Coca-Cola syrup, and using the name Coca-Cola thereon in the territory herein described.
>
> * * * * * * *
>
> [Bottler agrees] . . . Not to use the name Coca-Cola nor bottle nor vend said product except in the territory herein referred to without the written consent of party of the first part and The Coca-Cola Company. This limitation, however, is not to prevent party

> of the second part from obtaining such rights from parties authorized to use the name Coca-Cola and to bottle and vend said product. [28]
>
> * * * * * * *
>
> [Bottler agrees] . . . To order, for the purpose of bottling Coca-Cola, the distinctive bottle, and none other, adopted or that may be adopted by party of the first part; to use said distinctive bottle and none other, in bottling Coca-Cola, and not to use said distinctive bottle for any other purpose than the bottling of Coca-Cola, and not in any territory except as herein referred to without the written consent of party of the first part and The Coca-Cola Company.

(CXs 11–15, 20–23, 26, 29, 31–33.)

63. Bottlers do not ship their products to a food chain if they believe all, or part, of the product is going to be transshipped outside the bottler's territory. If they find that product which has been delivered to a chain or other customer has been transshipped outside the bottler's territory, the bottler undertakes to get the chain to stop such transshipment in the future (Smith, Tr. 595).

64. When bottlers have notified "Coca-Cola" that their exclusive territories have been violated, it has been the policy of "Coca-Cola" to bring the subject to the attention of the bottler from which the product was alleged to have come (Smith, Tr. 664).

65. Usually when the matter is brought to the attention of the trespassing bottler, such bottler does what he can to stop the practice (Smith, Tr. 665).

Bottlers sell only in their own territory for ultimate resale in the territory (Carver, Tr. 1606; Ellis, Tr. 965; Brendle, Tr. 1764; Navarre, Tr. 1522, 1526).

66. Bottlers are free to, and they do, independently of "Coca-Cola" establish their prices for their soft drink products in their defined geographic territories (Smith, Tr. 688–89; Stokes, Tr. 1128). They also are free to purchase "Coca-Cola" approved bottles and crowns, other supplies, vending machines, coolers, vehicles, cases, bottling equipment, etc., from whomsoever they choose and "Coca-Cola" receives no royalty, compensation, or commission (Smith, Tr. 653–54, 690–92). Obtaining approval is not difficult (Smith, Tr. 65). [29]

67. In deciding on their pricing and packaging, bottlers are aware that other Coca-Cola bottlers will not violate their territory or compete in price or in packaging (Stokes, Tr. 1123; Navarre, Tr. 1522–23; Massey, Tr. 2235; Filoromo, Tr. 2153).

68. Bottlers compete within their territories against national brands of soft drinks such as Pepsi-Cola, Seven-Up, Royal Crown, Canada Dry, Dr Pepper, and Shasta, and against regional brands such as Rock Creek, Faygo, and Vernor's private label brands (Stokes, Tr.

1109, 1112–1113; Ellis, Tr. 958–61; Massey, Tr. 2231–32; Filoromo, Tr. 2150–53).

69. Bottlers may and do choose whether they will engage in their own or participate in cooperative promotional efforts with "Coca-Cola" and other bottlers (Smith, Tr. 798–800; Stokes, Tr. 1121; Christian, Tr. 1825; Brown, Tr. 1681–82).

70. Bottlers may, and some do, produce brands other than those of "Coca-Cola." Many of them do not produce all of the "Coca-Cola" brands and do not package in all of the sizes (bottles) authorized by "Coca-Cola" (Sales, Tr. 1202, 1210; Navarre, Tr. 1495; Massey, Tr. 2224; Filoromo, Tr. 2124–25, 2173). If a bottler of Coca-Cola does not carry one or more of its allied products, "Coca-Cola" is free to license another bottler to manufacture, distribute and sell that soft drink brand in the territory of the bottler who declined to handle the brand (Smith, Tr. 675) although to date "Coca-Cola" has chosen not to do so (Smith, Tr. 675).

71. In 1971, 438 of the 726 licensed bottlers of "Coca-Cola" and the Thomas Companies were licensed to sell trademarked soft drink products other than those of "Coca-Cola" (Smith, Tr. 689).

72. Bottlers use a store-door delivery system and do not deliver to chain store warehouses (Brown, Tr. 1673; Navarre, Tr. 1516–17; Massey, Tr. 2228, 2232, 2240; Millard, Tr. 2300). [30]

73. The current average cost in the United States to deliver Coca-Cola and allied products in cans directly to individual supermarkets and to merchandise the product under the prevailing store-door delivery system used by bottlers is approximately the same ($.06 more per case) as the average cost of delivery and merchandising Coca-Cola through the food store warehouse delivery system (Cowart, Tr. 3361–62; RX 123). Cans are the easiest package to deliver through the warehouse system because cans are a compact, low cubage container (Cowart, Tr. 3362). This is indicated by the fact that cans are the predominant container delivered through the warehouse delivery system. Eighty percent of Shasta soft drinks (Meyers, Tr. 1737) and most private labels (Smith, Tr. 735) are sold in cans.

74. The difference between costs of the store-door delivery system and the warehouse delivery system in different parts of the country for delivering a case of cans would vary from three to five cents (Cowart, Tr. 3438). This difference is about 1 percent to 1 1/2 percent of the current wholesale price of a case of cans which, for example, is $4.77 in San Francisco (Cowart, Tr. 3425, 3438). The average cost in the United States to deliver Coca-Cola in 32-oz. non-returnable bottles through warehouses would be 9.6 cents more per case than the cost under the current store-door delivery system (Cowart, Tr. 3438–39).

The reason the costs of the store-door delivery system and the warehouse delivery system are approximately the same for non-returnable containers is that the same functions are performed under each system (Cowart, Tr. 3326–29, 3332–34; RX 121; RX 122).

75. The bottlers obtain canned trademarked soft drink products in the following ways. (1) Some bottlers have their own canning facilities. (2) Some bottlers have canned products produced for them by other bottlers under an agency canning agreement. (3) Some bottlers have formed canning cooperatives to produce canned products for their members. (4) Some bottlers obtain canned product from Canners for Coca-Cola Bottlers, Inc., a subsidiary of "Coca-Cola." Others obtain canned products from independent contract canners approved by "Coca-Cola" (Ogden, Tr. 834, 836, 837). [31]

76. A typical bottling line includes: (1) a system for cleansing the container, (2) a water purification system, (3) a carbonation system, (4) a system which mixes syrup in the correct ratio with water and carbonation supplied by supporting systems, (5) a filling system whereby the mixture is transferred to bottles in the correct amount, (6) a closure system for final capping of the finished product, and (7) ancillary systems which case and transfer finished products in accordance with the requirements of the particular operation (Smith, Tr. 586–87).

77. Bottlers' facilities are inspected by "Coca-Cola" on the average of three to four times a year (Sales, Tr. 1239-40; Alford, Tr. 2491; Hornsby, Tr. 3153–54). These inspections are generally unscheduled and unannounced (Susong, Tr. 921; Rooks, Tr. 1379; Bernabucci, Tr. 1980; Millard, Tr. 2326). They have included water analysis, bacteriological checks on water and processing equipment, measure of syrup content and degree of carbonation, bottle washing solution checks, and sanitation monitoring (Ellis, Tr. 973; RX 33A–J). Quality control inspectors also visit retail outlets and purchase products for analysis (Susong, Tr. 921; Ellis, Tr. 974–75). In addition, each production facility is required to submit monthly samples of every product to a quality control laboratory of "Coca-Cola" (Rooks, Tr. 1379–80; Alford, Tr. 2491–92; Hornsby, Tr. 3153). Many production facilities have their own laboratories, chemists, and quality control personnel (Ellis, Tr. 975–76; Millard, Tr. 2325–26; Alford, Tr. 2480–81; Crabtree, Tr. 2669). Inspections conducted by "Coca-Cola" were characterized as "more stringent" than governmental inspection by state authorities and the Food and Drug Administration (LaDoux, Tr. 1468). On occasion "Coca-Cola" has notified bottlers of Coca-Cola that it would cancel their contracts if substandard quality conditions were not corrected (Susong, Tr. 911–12).

78. Bottlers of Coca-Cola rotate the stock on retail shelves to insure that the product does not get old and that the consumer purchases a fresh-tasting drink (Smith, Tr. 698; Ellis, Tr. 979; Sales, Tr. 1241, 1310–11; Rooks, Tr. 1373; LaDoux, Tr. 1465; Carver, Tr. 1632; Christian, Tr. 1857; Millard, Tr. 2324; Roadcap, Tr. 2454; Burks, Tr. 3008). Route salesmen check the date code marked on the product (Ellis, Tr. 979; Sales, Tr. 1241; Rooks, Tr. 1373; Carver, Tr. 1632). Flavored [32] carbonated soft drinks do not contain preservatives (Smith, Tr. 698; Ellis, Tr. 978). Most people familiar with the soft drink industry agree that soft drink products have a definite shelf life, a span of time beyond which the taste begins to noticeably deteriorate (Smith, Tr. 698). This deterioration affects taste but does not present a danger to health (Smith, Tr. 698; Ellis, Tr. 978). Deterioration results from the process of oxidation, which varies depending on exposure to heat and light (Ellis, Tr. 978–79). Estimates of this span are variously given for bottled products as two to four weeks (Stokes, Tr. 1111–17), three to eight weeks (Sales, Tr. 1240–41), sixty days (Carver, Tr. 1632), a few weeks (Ellis, Tr. 979), a month or so (Cameron, Tr. 2087), and four to eight weeks for bottles and 25 days for cans if stored in a cool, dark place (Rooks, Tr. 1381). The shelf life of cans depends on whether the cans are made of steel or aluminum. Aluminum cans retain taste quality a little longer than steel cans and do not transmit a metallic flavor to the drink (Stokes, Tr. 1116–17; Sales, Tr. 1240–41, 1343–44; Millard, Tr. 2300). The taste of flavored carbonated soft drinks becomes "unbearable" in eight to ten weeks in steel cans (Sales, Tr. 1343–44).

79. If despite stock rotation old product is discovered at a retail outlet, route salesmen are instructed to replace the product and bring the old product back to the plant for disposal (Ellis, Tr. 979; Sales, Tr. 1311; Rooks, Tr. 1381; Carver, Tr. 1632; Roadcap, Tr. 2454).

80. The plant inspection and the submission of product samples (Cobetto, Tr. 2833–34; Strachan, Tr. 2878–79; Ippolito, Tr. 3245; Hurst, Tr. 3453; Clements, Tr. 3989) and stock rotation by bottlers' route salesmen (Cobetto, Tr. 2834; Strachan, Tr. 2893; Ippolito, Tr. 3248) are employed by other national brand soft drink licensors and their bottlers.

81. The distributional system of every licensed bottler of Coca-Cola is predicated upon store-door delivery and the direct servicing of all accounts (Smith, Tr. 655–56). [33]

82. Coca-Cola is distributed widely by bottlers and is available for purchase by consumers, often through vending machines owned by bottlers or others, through such outlets as:

Supermarkets
Convenience Stores
Small Grocers
Other Food Stores
Drug Stores
Service Stations
Department Stores
Discount Stores
Variety Stores
Sports Arenas
Civic Centers and Auditoriums
Golf Courses
Amusement Parks
Bowling Alleys
Ice and Roller Rinks
Hotels & Motels
Airports
Train Stations/Depots
Bus Stations/Depots
Bars and Taverns
Restaurants
Luncheonettes
Drive-Ins
Cafeterias
Snack or Specialty Shops
Offices
Industrial Plants
Schools
Hospitals and Nursing Care Homes
Prisons, and Retail Establishments not listed above (*e.g.*, beauty salons, barber shops, liquor stores, home delivery vendors and movie theaters).

(Stipulation No. 5, RX 2-Z41-Z42.)

83. While chain store accounts usually represent from 20 to 30 percent of a bottler's business, they constitute only a minute fraction of the bottler's delivery stops (Smith, Tr. 660).

84. Licensed bottlers of "Coca-Cola" service many unprofitable accounts in order to have the product available in as many outlets as possible (Smith, Tr. 700). (See Findings 137-148, 174-178 below.) [34]

85. The bottler of Coca-Cola in Annapolis, Maryland, obtained a 3.7 percent return on investment after taxes in 1974 (Brendle, Tr. 1789), which return was greater than that obtained in 1973 (Brendle, Tr. 1786). The Coatesville Coca-Cola Bottling Works, Inc. has been profitable since its inception in 1917 (Filoromo, Tr. 2196), but did not pay a dividend until 1935 (Filoromo, Tr. 2160), and still pays "meager" dividends today (Filoromo, Tr. 2199). The Filoromo family, which owns Coatesville Bottling Works, works on small salaries and makes a return on invested capital of 2 1/2 - 3 percent after taxes (Filoromo, Tr. 2197). The James E. Crass Coca-Cola Bottling Plants, Inc., with plants in Washington, D.C., Richmond, Virginia, Frederick, Maryland, and elsewhere, pays dividends of 2 - 3 percent on book value, which percentage would be much lower if based on market value of the investments (Stokes, Tr. 1076). The bottler of Coca-Cola in Hartwell, Georgia, made an after-tax profit of $46,000 (Rooks, Tr. 1406) and its

two owners receive monthly salaries of $1,000 and $1,250, respectively (Rooks, 1407). The bottler of Coca-Cola in Spirit Lake, Iowa, made a profit during 14 of the last 17 years, which profit level has never been in excess of four percent of sales (LaDoux, Tr. 1478–79). The Spirit Lake bottler was profitable last year, obtaining a two percent return on sales (LaDoux, Tr. 1478–79), barely profitable the year before, and unprofitable two years ago (LaDoux, Tr. 1475). The bottler of Coca-Cola in Newport News has been profitable since 1914 and obtains a return on investment below five percent (Brown, Tr. 1701). The Coca-Cola Bottling Company of New York, Inc., a publicly held bottler, has a current return on equity of 6.4 percent (Millard, Tr. 2357–58). The bottler of Coca-Cola in Ada, Oklahoma has obtained a 3 – 4 percent return on book value for the last few years (Crabtree, Tr. 2684) and achieves a 10 cent per case profit before taxes (Crabtree, Tr. 2684). The bottler of Coca-Cola in Jamestown, North Dakota, receives a 7 – 8 percent return after taxes on the replacement value of his investments (Bernabucci, Tr. 1973–74). The salaries taken by bottlers and their rates of return on invested capital and sales are reasonable. [35]

86. Effective interbrand competition has also kept the profits of bottlers of other national brands at a reasonable level. The Pepsi-Cola bottler in Albany, New York, obtains a 4 1/2 percent return on the market value of his investments (Strachan, Tr. 2873). The Dr Pepper-Pepsi-Cola bottler in Dyersburg, Tennessee obtains a five percent before tax return on the replacement value of the company's assets (Burks, Tr. 3047), takes less than $20,000 in salary (Burks, Tr. 3047), has paid only $16,000 in dividends since 1965 (Burks, Tr. 3046–47), and makes a per case profit of only 13 to 14 cents before taxes (Burks, Tr. 3048). The Dr Pepper bottler in Galveston, Texas, makes a profit of $40,000 on sales of $1,600,000 (Ippolito, Tr. 3271–72), obtains a five percent return on the market value of his investments (Ippolito, Tr. 3268), makes a profit of 15 to 20 cents per case before taxes (Ippolito, Tr. 3267), and has not paid any dividends in the last decade (Ippolito, Tr. 3267).

87. When family-owned bottlers of Coca-Cola have decided that they no longer wish to remain in the bottling business, they have been and are free to sell their exclusive trademark license to bottle and sell Coca-Cola in a given territory. "Under the existing system, if it becomes inefficient or unprofitable for a bottler to continue to serve his area, or when the members of a family decide that they no longer wish to remain in the bottling business, they can sell their franchise, as well as their plant and equipment" (Smith, Tr. 614). "Usually a bottler can afford to pay his neighboring bottler a generous price for his territory" and "the bottler who sells his plant is usually assured that he

will receive a fair and equitable compensation for the investment he has made in developing his territory" (Smith, Tr. 616). Bottlers can acquire another bottler without the approval of "Coca-Cola" through a stock acquisition (Smith, Tr. 628). "Coca-Cola," if asked, has recommended that bottlers merge or consolidate where appropriate (Smith, Tr. 615–16). However, bottlers are independent businessmen who make their own independent decisions and who frequently act contrary to the advice of "Coca-Cola" (Smith, Tr. 615–16). [36]

Competition in the Soft Drink Industry

Generally

88. There is intense competition in the sale of flavored carbonated soft drinks which stems from the fact that there is a large number of brands available to the consumer in local markets. In 1971, a Neilsen Survey showed that there were 135 different brands of cola flavored soft drinks marketed in food stores (Smith, Tr. 705). In the Washington, D.C., metropolitan area alone, there are over 30 brands of colas being marketed (Sales, Tr. 1243–1251). In addition to the cola brands, more than 20 other brands of flavors such as root beer, orange, gingerale, and lemon-lime were being sold in the Washington, D.C., market (Sales, Tr. 1243, 1255; CX 372; CX 373). In the territory of the Newport News, Virginia bottler of Coca-Cola, between 30 and 40 different brands of orange and grape soft drinks were being marketed (Brown, Tr. 1666). Over 176 different brands of flavored carbonated soft drinks were sold in the territory of The Coca-Cola Bottling Company of New York, Inc. (Millard, Tr. 2347).

89. The consumer has a substantial number of brands available from which to choose in large urban areas, small towns, and rural communities alike. For example, over 40 different brands in the areas around Elmira (RX 78A–E), and Syracuse, New York (RX 83A–G); over 35 different brands in the areas around Richmond, Virginia (CX 364A–C; CX 367A–B), Utica (RX 84A–D), Watertown (RX 85A–D), and Binghamton, New York (RX 76A–C); over 30 different brands in the areas around Philadelphia (RX 73A–D), Fredericksburg, Virginia (CX 365; CX 368A–B), Petersburg, Virginia (CX 366; CX 369A–B), Frederick, Maryland (CX 362A–B), Westminster, Maryland (RX 53A–C), Cortland (RX 77A–C), Finger Lakes (RX 79A–D), Gloversville (RX 80A–C), and Oneonta, New York (RX 82A–D); and over 20 different brands in Camden, New Jersey (RX 73E–F), Albany (RX 74A–C), Glens Falls (RX 75A–C) and Hudson, New York (RX 81A–B). Many brands are marketed in a number of different flavors. At a given retail outlet, it is not uncommon for the consumer to also have a choice of 25–30

flavors, both in dietetic and regular form (Stip. No. 3, CX 1244K, Tr. 479). [37]

90. The degree of competition in the industry both nationally and in over two dozen local markets was described by various witnesses in the business as follows: "very active" (Smith, Tr. 707); "highly competitive" (Ellis, Tr. 986); "fierce," "intense," and "tremendous" (Sales, Tr. 1242, 1332); "very aggressive" (LaDoux, Tr. 1458); "bloody, fierce" (Navarre, Tr. 1536); "extensive" (Brown, Tr. 1697); "strenuous" (Brendle, Tr. 1781); "quite intense" (Levin, Tr. 1912); "severe competitive situation" (Filoromo, Tr. 2179); "vicious, intense, heated," "most competitive business I have ever seen" (Millard, Tr. 2351–53); "high[ly] competitive" (DeLap, Tr. 2576); "very, very competitive" and "very, very intense" (Crabtree, Tr. 2673, 2679); "very intense" (Cobetto, Tr. 2827); "fierce" (Strachan, Tr. 2885–86); "brutal" (Connellee, Tr. 2965); "terrific," "aggressive" (Ippolito, Tr. 3233–34, 3264–65); "more competitors . . . than anywhere in the supermarket" (Reid, Tr. 3560); "the most competitive industry," "very intensive, very fierce and very vigorous" (Clements, Tr. 4024).

91. The testimony of witnesses familiar with the soft drink industry was that such competition was increasing. (Smith, Tr. 707–08; Ellis, Tr. 986; Sales, Tr. 1243; Navarre, Tr. 1536; Brendle, Tr. 1781; Levin, Tr. 1912–13; Cameron, Tr. 2057; Filoromo, Tr. 2180; Alford, Tr. 2508; Delap, Tr. 2576; Sheldon, Tr. 2615; Strachan, Tr. 2886; Reid, Tr. 3560.)

Brand Competition

92. "Coca-Cola" and allied products sold by bottlers of Coca-Cola compete against a wide variety of national brand flavored carbonated soft drinks. Among the national brand products with which bottlers of Coca-Cola and allied products testified they compete in various local markets are Pepsi-Cola (Ogden, Tr. 839; Stokes, Tr. 1170; LaDoux, Tr. 1456; Carver, Tr. 1610; Levin, Tr. 1899) and other products of the Pepsi-Cola Company such as Diet Pepsi (Brown, Tr. 1684; Alford, Tr. 2501), Patio flavors (Millard, Tr. 2344) and Mountain Dew (Rooks, Tr. 1388; Brendle, Tr. 1774); Seven-Up (Smith, Tr. 705; Stokes, Tr. 1170; Rooks, Tr. 1388; Brown, Tr. 1684; [38] Brendle, Tr. 1774; Christian, Tr. 1834) and other products of the Seven-Up Company such as Howdy Cola (RX 73B) and Diet Seven-Up (Millard, Tr. 2344; Alford, Tr. 2501); Dr Pepper (Rooks, Tr. 1388; LaDoux, Tr. 1456; Carver, 1610) and Sugar Free Dr Pepper (Millard, Tr. 2344); Canada Dry (Rooks, Tr. 1388; Brendle, Tr. 1774; Christian, Tr. 1834; Cameron, Tr. 2057; Filoromo, Tr. 2151; Massey, Tr. 2231) and other products of the Canada Dry Corporation such as Jamaica Cola (Sales, Tr. 1251) and Wink (Carver,

Tr. 1611); Royal Crown (Ogden, Tr. 839; Stokes, Tr. 1170; Navarre, Tr. 1514–15; Christian, Tr. 1834; Levin, Tr. 1899) and other products of the Royal Crown Cola Co. such as Par-T-Pak (Carver, Tr. 1611), Diet Rite (Stokes, Tr. 1146; Rooks, Tr. 1388; Alford, Tr. 2501) and Nehi flavors (Stokes, Tr. 1146; Alford, Tr. 2501–02); Schweppes (Ellis, Tr. 985; Brown, Tr. 1684); Squirt (Ellis, Tr. 985); NuGrape (Wimberly, Tr. 875); London Dry (Rooks, Tr. 1388); YooHoo (Rooks, Tr. 1388; Levin, Tr. 1899) and Brownie (Brown, Tr. 1684) chocolate sodas; Dixi Cola (Sales, Tr. 1250); Climax gingerale (Carver, Tr. 1610; Brown, Tr. 1684); Lipton (Sales, Tr. 1252) and Nestea (Crabtree, Tr. 2676) canned iced teas; Frostie (Stokes, Tr. 1146; Alford, Tr. 2502), Dad's (Stokes, Tr. 1146), Hires (Levin, Tr. 1899), Ma's Old Fashioned (Filoromo, Tr. 2152) and A&W (Levin, Tr. 1899) root beers; Orange Crush (Levin, Tr. 1899; Bernabucci, Tr. 1983; Massey, Tr. 2230); No Cal (Stokes, Tr. 1146; Filoromo, Tr. 2151; Millard, Tr. 2344); Weight Watchers (Levin, Tr. 1899); Tru-Ade (Stokes, Tr. 1146; Carver, Tr. 1610); Double Cola (Sales, Tr. 1248; DeLap, Tr. 2576; Crabtree, Tr. 2676); Triple Cola (Stokes, Tr. 1147); Cliquot Club (Sales, Tr. 1250); White Rock (Stokes, Tr. 1147; Millard, Tr. 2344); Snow Peak (Stokes, Tr. 1147); C&C Cola (Stokes, Tr. 1147; Millard, Tr. 2344); Wild West Sasparilla (Brown, Tr. 1684); and Shasta (Wimberly, Tr. 875; LaDoux, Tr. 1456; Carver, Tr. 1611). Bottlers of Pepsi-Cola (Strachan, Tr. 2883–84), Dr Pepper (Burks, Tr. 3035–36; Ippolito, Tr. 3243, 3256, 3265), and Seven-Up and Royal Crown (Cobetto, Tr. 2825) as well as witnesses selling Dr Pepper (Clements, Tr. 3987, 4015); Shasta (Meyers, Tr. 1724, 1727, 1733); and Lipton (Reid, Tr. 3562–63) and Nestea (Hurst, Tr. 3455–56) canned iced teas testified that their respective products compete with Coca-Cola and allied products as well as other national brand flavored carbonated soft drinks. [39]

93. In most local markets, bottlers of Coca-Cola and other national brands compete with local and regional brands of flavored carbonated soft drinks manufactured and sold by independent producers under their own labels (Stip. No. 3, CX 1244E, Tr. 474). The brands of these local and regional manufacturers, such as Blair House and Rock Creek in Washington, D.C., Suburban Club in Baltimore, Frank's in Philadelphia, Graf's in Milwaukee, and Faygo and Vernor's in Detroit, have been strong competitors in specific markets for decades (Stip. No. 3, CX 1244E, Tr. 474).

94. Other local and regional brands of flavored carbonated soft drinks with which Coca-Cola and allied products compete include Canfield's in Chicago (Ogden, Tr. 839; Meyers, Tr. 1732); Frank's in Pennsylvania, Maryland, Delaware, Virginia, and the District of Columbia (Ellis, Tr. 984; Stokes, Tr. 1146; Sales, Tr. 1249; Carver, Tr.

1611; Levin, Tr. 1899; Massey, Tr. 2231; Roadcap, Tr. 2423); Hoffman's in Maryland, Virginia, Pennsylvania, and New York (Ellis, Tr. 985; Stokes, Tr. 1146; Meyers, Tr. 1733; Christian, Tr. 1899; Millard, Tr. 2344); Suburban Club in Maryland and Virginia (Ellis, Tr. 985; Stokes, Tr. 1146; Carver, Tr. 1610); Rock Creek (Sales, Tr. 1249; Brendle, Tr. 1780) and Blair House (Sales, Tr. 1249; Brendle, Tr. 1780) in the greater Washington, D.C., area; Green Spot, A-Treat, Reading Beverages, and Crystal Beverages in the Reading, Pennsylvania, area (Levin, Tr. 1899); Ritz in Florida (Meyers, Tr. 1732); Mission in San Antonio and the Southwest (Meyers, Tr. 1733; Alford, Tr. 2505); Checkers in Louisville (Meyers, Tr. 1733); Texas Beverages in San Antonio (Roadcap, Tr. 2482); Belfast in the San Francisco area (Sheldon, Tr. 2614); White Rock in New York and New Jersey (Millard, Tr. 2344); Regent in Pittsburgh (RX 2Z34); and Variety Club in Toledo (RX 2Z10). Various regional brands were described as a "very strong competitor" (Suburban Club) (Ellis, Tr. 985), "tough competitors" (regional brands collectively) (Meyers, Tr. 1732), and "tremendous competitors" (Faygo and Shasta) (Cameron, Tr. 2058). In fact, the bottler of Coca-Cola in San Antonio had The Coca-Cola Company develop a red cream soda, "Fanta Red," in order to compete with the strong market performance in the area of "Big Red," a local red cream soda brand (Alford, Tr. 2482, 2502–04). Big Red retails at the same price as Coca-Cola and has 10 percent of the home market (Alford, Tr. 2502–03). [40]

95. Shasta, which is produced by Consolidated Foods Corp. and which 10 years ago was confined to the West Coast, has now become a national brand marketed in all 50 states (Smith, Tr. 707; Meyers, Tr. 1710–14; Stip. No. 3, CX 1244E, Tr. 474). Shasta, in 1971, on the basis of estimates by Neilsen, was the fourth ranked brand in food stores in San Francisco, San Jose, Fresno, Seattle, Spokane, Tacoma, Portland, Baton Rouge, Las Vegas, Denver, Reno, Phoenix, Kansas City, and St. Louis (RX 2Z–2Z1).

96. Physical case sales of Shasta brand flavored carbonated soft drinks nationally and in the New York-Virginia corridor area in the years indicated were as follows:

Year	*N.Y.-Va. Corridor*	*United States*
1967	493,000	17,645,000
1970	1,008,000	35,676,000
1972	4,629,000	56,992,000

(Stip. No. 7, RX 102Z16).

97. Shasta soft drink products are priced below the prices of

national soft drink brands and above the prices of private label soft drink products (Meyers, Tr. 1751).

98. Bottlers of Coca-Cola and other national brands also compete with private label soft drinks which, since the early 1960's, have become a substantial competitive force in the soft drink industry. Private label soft drinks are sold by a retailer under the retailer's own trade name or under a trade name of a wholesaling or other organization from which the retailer purchases, *e.g.*, 7-Eleven, Yukon Club (A&P), and Gayla (Topco) soft drinks. Private labels are manufactured either by the retailer or wholesalers themselves or for such firms by contract bottlers or canners. Private labels are generally sold for home consumption in non-returnable bottles and cans (Stip. No. 3, CX 1244F, Tr. 474–75). Private label soft drinks are sold by food chains, independent grocers, drug stores (Sales, Tr. 1247–48; Brown, Tr. 1683; Connellee, Tr. 2965), convenience stores (Sales, Tr. 1247; Navarre, Tr. 1520; Connellee, Tr. 2965), dairy stores (Sales, Tr. 1247), [41] restaurant chains (Sales, Tr. 1246–47), and others. In fact, many food chains now sell more than one private label (Ellis, Tr. 983; Sales, Tr. 1243–45; Navarre, Tr. 1518–19; Brendle, Tr. 1775; Filoromo, Tr. 2151–52; Hornsby, Tr. 3176). Nationally, literally hundreds of new private label soft drinks have entered the market, many in the last five years (Stip. No. 3, CX 1244F, Tr. 475). In the East, sales of private label flavored carbonated soft drinks by contract canners grew "dramatically" between 1964 and 1971 in part because more food chains went into the sale of private labels (Hornsby, Tr. 3173).

99. Coca-Cola and allied products and other national brand flavored carbonated soft drinks compete with a wide variety of private labels in virtually every market (Smith, Tr. 705; Sales, Tr. 1244–48; LaDoux, Tr. 1456; Navarre, Tr. 1518–20; Millard, Tr. 2346–48; Roadcap, Tr. 2424–25; Alford, Tr. 2504–05; DeLap, Tr. 2576; Strachan, Tr. 2885; Clements, Tr. 4015).

100. In smaller communities there are typically between four and ten private label soft drinks being marketed which compete with Coca-Cola and allied products. For example, in Richmond, Virginia, Coca-Cola and allied products compete with A&P's "Yukon Club," Giant Foods' "Glee," Safeway's "Cragmont," Grand Union's "Penguin," Colonial Stores' "Zesty," Food Fair's "Pantry Pride" and "Hy Tyme," and 7–11 convenience store's "7–11" brand (Stokes, Tr. 1114; CX 364A; CX 366). In Annapolis, Maryland, the bottler of Coca-Cola competes with Giant Foods' "Giant" and "Glee" brand private labels, Safeway's "Cragmont," A&P's "Yukon Club," Pantry Pride's "Pantry Pride" and "Fyne Taste," and Acme's "Bala Club" and "Ideal" brands (Brendle, Tr. 1775). In Wilmington, Delaware, Coca-Cola and allied products

compete with Acme's "Ideal," "Super Saver," and "Bala Club," Penn Fruit's "Gayla," Pantry Pride's "Pantry Pride" and "Hy Tyme," A&P's "A-brand," "Bond Street," and "Yukon Club," Shop Rite's "Shop Rite" brand, Pathmark's "Pathmark" private label, and "7-11" (Navarre, Tr. 1518–19; RX 32). [42]

101. Bottlers of Coca-Cola in Charlottesville, Virginia (Christian, Tr. 1839–41); Jamestown, North Dakota (Bernabucci, Tr. 1983–84); Westminster, Maryland (Roadcap, Tr. 2424–25); Coatesville, Pennsylvania (Filoromo, Tr. 2151–52); Montross, Virginia (Carver, Tr. 1611, 1614–16); and Dover, Delaware (Massey, Tr. 2234), testified that they compete with a number of private label brands.

102. Private label brands are a substantial competitive force. Nationally, Neilsen estimates that 20 percent of flavored carbonated soft drink sales in food chains are private label brands and that 40 percent of the sales of canned soft drinks are private labels (Smith, Tr. 705–06). The same source also estimates that private labels account for approximately 40 percent of all flavored carbonated soft drinks sold in food stores in the Washington, D.C., area (Sales, Tr. 1275) and approximately 30 percent in the New York metropolitan area (Millard, Tr. 2348).

Competition in Prices

103. There is price competition between Coca-Cola and allied products and other brands of flavored carbonated soft drinks (Smith, Tr. 742, 744; Sales, Tr. 1238, 1258–59; Rooks, Tr. 1362; Navarre, Tr. 1537–38). This pricing competition was described as "intense" (Levin, Tr. 1912; Reid, Tr. 3562) and "very tough" (Smith, Tr. 742). There is also very intense price competition from regional brands. For example, C&C Cola increased its market share in food stores in metropolitan New York from not being traceable in 1970 and 1972 to 3.6 percent of the market in 1975 (Millard, Tr. 2358). However, as a result of the exclusive territory provisions, competition *between licensed Coca-Cola bottlers* has been eliminated in their pricing of soft drinks, in the packaging of products, the sizes of containers and in the services they provide, such as warehouse delivery and pick-up at the bottling plant (Smith, Tr. 672–77). [43]

104. Because of keen interbrand price competition, bottlers of Coca-Cola attempt to price Coca-Cola and allied products at a level equal to or below major national brand competitors (Alford, Tr. 2483). In May 1975, Coca-Cola was priced below Pepsi-Cola in such markets as Washington, D.C. (Sales, Tr. 1238), Humbolt, Iowa (LaDoux, Tr. 1459), Westminster, Maryland (Roadcap, Tr. 2443), Montross, Virginia (Carver, Tr. 1630), Charlottesville, Virginia, (Christian, Tr. 1854–56),

Newport News, Virginia (Brown, Tr. 1671–A), and Coatesville, Pennsylvania (Filoromo, Tr. 2180). When Coca-Cola is priced below Pepsi-Cola and other competing brands, as happened in Charlottesville between November 1974 and May 1975, sales of Coca-Cola improve substantially at the expense of the other brands (Christian, Tr. 1854–56). These other national brands view competitive pricing as important (Burks, Tr. 3046; Clements, Tr. 4024), and the Dr Pepper bottler in Dyersburg, Tennessee, indicated that he could not afford to sell at a retail price of even one, two or three cents higher on a six pack than Coca-Cola and other national brands for an extended period of time (Burks, Tr. 3046). The bottler of Coca-Cola in San Antonio testified that his sales will be adversely affected if his prices are two or three cents higher on a six pack (Alford, Tr. 2483), and the licensor of Nestea canned iced tea testified that even a one cent difference on a six pack may affect consumer choice (Hurst, Tr. 3457).

105. During late 1973 and 1974, there was a substantial increase in the price of sugar (Brown, Tr. 1694; Cameron, Tr. 2056; Sheldon, Tr. 2616; Clements, Tr. 4017), which is one of the principal ingredients in flavored carbonated soft drinks, and there also were increases in container and other costs (Brown, Tr. 1694). These increases in the cost of ingredients and containers brought about a substantial increase in the prices of flavored carbonated soft drinks (Brown, Tr. 1693–94; Sheldon, Tr. 2616; Clements, Tr. 4017). In 1974, home market sales of flavored carbonated soft drinks declined for the first time (Clements, Tr. 4016) as the substantial increase in the price of flavored carbonated soft drinks resulted in consumers purchasing powdered mixes and other types of beverages (Clements, Tr. 4016–17). [44]

106. The prices charged by bottlers of Coca-Cola and allied products are determined by the prices of competing brands, costs of ingredients, and containers (Ellis, Tr. 965; Sales, Tr. 1259–60, 1324; Carver, Tr. 1617, 1640; Millard, Tr. 2310). Such competition also controls the prices charged by bottlers of Dr Pepper (Clements, Tr. 4024) and other national brand soft drinks (Cobetto, Tr. 2836). When costs of ingredients and containers are relatively stable, bottlers of Coca-Cola have been able to maintain their price levels. For example, the wholesale prices charged by Washington Coca-Cola Bottling Company did not rise from April 1, 1971, until April 1, 1974 (Sales, Tr. 1260).

107. Because of competition from other brands when the cost of sugar forced the price of sweetened flavored carbonated soft drinks to increase, many bottlers of Coca-Cola did not correspondingly increase the price for diet flavored carbonated soft drinks which do not contain sugar (Carver, Tr. 1625; Cameron, Tr. 2091–92; Roadcap, Tr. 2448–49).

The result was a 30 to 50 cent per case differential between diet and sugar sweetened flavored carbonated soft drinks (Carver, Tr. 1625; Roadcap, Tr. 2448–49). Because of a reduction in the price of sugar in 1975, bottlers of Coca-Cola began to reduce their wholesale soft drink prices (Rooks, Tr. 1385; Cameron, Tr. 2056; Sheldon, Tr. 2617; RX 68).

108. When prices charged by bottlers of Coca-Cola are above those charged by major competitors such as Pepsi-Cola, sales of Coca-Cola decline. In early 1973, the effective price of Pepsi-Cola fell below Coca-Cola in New York City. The result was that the home market share average of Coca-Cola over Pepsi-Cola declined from 18 versus 11 percent to 14 versus 12 percent. This forced The Coca-Cola Bottling Company of New York to increase pricing and promotion expenditures from $7–8 million to $17 million to recapture its position (Millard, Tr. 2355–57). In Hartwell, Georgia, loss of market share forced the bottler of Coca-Cola to meet the quantity discounts offered by his Pepsi-Cola competitor (Rooks, Tr. 1391–92). Similarly, when as a result of increased sugar prices Coca-Cola Bottling Company of the Peninsula in California found itself to be premium priced over Pepsi-Cola [45] and other national brands for the first quarter of 1975, the price differential led to a considerable slowdown in sales of Coca-Cola. The result was that Coca-Cola "priced [itself] out of the market place" (Sheldon, Tr. 2616–17). When Coca-Cola Bottling Company of the Peninsula reduced its price in March 1975 (Sheldon, Tr. 2617; RX 68), sales of Coca-Cola significantly increased (Sheldon, Tr. 2620).

109. The wholesale prices charged by bottlers of Coca-Cola are competitive with the wholesale prices charged by their national brand competitors in the same local markets. On July 15, 1971, for example, the regular wholesale prices for a case of 24 12-ounce cans of Coca-Cola and Pepsi-Cola were $3.00 each in Annapolis (CX 453A; RX 103I); $3.00 each in Charlottesville (CX 431; RX 103X); $3.00 each in Montross, Virginia (CX 387B; RX 103Z1); $3.00 each in Westminster, Maryland (CX 991; RX 103Z1); $3.25 each in Albany, New York (CX 929; RX 103T); $3.10 each in Elmira, New York (CX 929; RX 103S); $3.25 each in Glens Falls, New York (CX 929; RX 103R); $3.25 each in Syracuse, New York (CX 929; RX 103Z2); $3.10 each in Binghamton, New York (CX 929; RX 1030); $3.00 each in Philadelphia (CX 694; RX 103V); and $3.10 each in Watertown, New York (CX 929; RX 103N).

110. The most economical packages sold by bottlers of Coca-Cola and other national brands in almost every market are the larger size returnable bottles, namely the 16-ounce returnable (Smith, Tr. 770; Stokes, Tr. 1140–41; Sales, Tr. 1261, 1338–39; LaDoux, Tr. 1459, 1461; Brendle, Tr. 1773; Christian, Tr. 1822–23, 1863; Levin, Tr. 1925, 1940; Filoromo, Tr. 2148; DeLap, Tr. 2579; Connellee, Tr. 2971) and the 32-

ounce returnable/resealable (Stokes, Tr. 1141; LaDoux, Tr. 1459; Navarre, Tr. 1540; Carver, Tr. 1631; Christian, Tr. 1861; Ippolito, Tr. 3249–50). Even bottlers who do not distribute returnables (Strachan, Tr. 2870–72) or who sell only a small percentage of returnables (Millard, Tr. 2305) testified that the returnable bottle with a reasonable trippage was the "most economical" package for the consumer. [46]

111. The returnable bottle is the most economical package to the consumer because the higher cost of the returnable container itself is spread over a large number of trips which the bottle makes before it is lost, destroyed or is no longer usable (Ellis, Tr. 997). For example, a 16-ounce returnable bottle which costs 12 cents, and which makes 18–20 trips before it is lost or destroyed, averages out to a container cost of only a fraction of a cent per trip (LaDoux, Tr. 1461–62; Alford, Tr. 2488; Clements, Tr. 3996). On the other hand, when a consumer buys a non-returnable bottle, the full cost of the container must be recovered in the purchase price of the beverage (Clements, Tr. 3996, 4042; RX 16).

112. Container costs are a substantial part (often over 50 percent) of the total cost of flavored carbonated soft drinks sold in non-returnable containers (Hornsby, Tr. 3177). In May 1975, a case of 24 empty 12-ounce conventional steel cans cost $1.44 or 6 cents per can (LaDoux, Tr. 1461–62). The cost of aluminum cans is almost identical to conventional steel cans (Sales, Tr. 1342–43).

113. Nationwide, approximately 55 percent of the sales of Coca-Cola in bottles and cans on a volume basis is sold in returnable bottles (Smith, Tr. 661, 777–78; Teasley, Tr. 3633, 3653, 3755). The percentage of soft drinks sold in returnable bottles varies in different areas of the country (Teasley, Tr. 3758–59, 3777–78; RX 7). Fifty percent of the sales of Coca-Cola in bottles and cans in Richmond are packaged in returnable bottles (Stokes, Tr. 1115, 1167); 30 percent in Washington, D.C. (Stokes, Tr. 1167); 65 percent in Hartwell, Georgia (Rooks, Tr. 1384); 70 percent in Spirit Lake, Iowa (LaDoux, Tr. 1462) and the State of Iowa generally (LaDoux, Tr. 1463); 30 percent in Wilmington, Delaware (Navarre, Tr. 1541–42); 25 percent in Havre de Grace, Maryland (Navarre, Tr. 1542); 75 percent in Charleston, West Virginia (Navarre, Tr. 1542); 54 percent in Miami (Navarre, Tr. 1542); 74 percent in Montross, Virginia (Carver, Tr. 1633); 60 percent in Charlottesville, Virginia (Christian, Tr. 1859); 40 percent in Reading, Pennsylvania (Levin, Tr. 1916); 65 percent in Washington, Pennsylvania (Cameron, Tr. 2042); 20 percent in Coatesville, Pennsylvania (Filoromo, Tr. 2172); 47.9 percent in Westminster, Maryland (Roadcap, Tr. 2448); 41 percent in Dover, Delaware (Massey, Tr. 2226); 51 percent in San Antonio, Texas (Alford, Tr. 2487); 45 percent in Stockton,

California (DeLap, Tr. 2567); 55–57 percent in Palo Alto, Burlingame and San Mateo, California (Sheldon, Tr. 2610); 60 percent in Jamestown, North Dakota (Bernabucci, Tr. 1982) and 70 percent in Ada, Oklahoma (Crabtree, Tr. 2670). [47]

114. There has recently been a resurgence of the use of returnable bottles and it appears that the share of the total soft drink market accounted for by returnable bottle sales has stabilized (Smith, Tr. 604, 609, 661–62; Strachan, Tr. 2872; Teasley, Tr. 3640, 3645–46). The percentage of Coca-Cola sold in returnable bottles has risen in Richmond, Virginia (Stokes, Tr. 1179–80), is increasing in Miami, Florida, and Wilmington, Delaware (Navarre, Tr. 1542), and reverted from 45 percent returnable/55 percent non-returnable to 55 percent returnable/45 percent non-returnable in the territory of The Coca-Cola Bottling Company of the Peninsula in California (Sheldon, Tr. 2610). The principal reasons that the share of the market may have stabilized are adjustments in the deposit structure and the increasing segmentation of the market to the point where economy oriented purchasers are buying returnable bottles and convenience buyers are purchasing convenience packages rather than buying returnables and discarding them (Teasley, Tr. 3640). The introduction of the 32-ounce returnable also helped arrest the decline in returnable bottle sales (Smith, Tr. 662). In the immediate future, there are no market forces or trends in consumer preferences which are likely to bring about a substantial change in the share of soft drink volume accounted for by sales of returnable bottles (Teasley, Tr. 3650–51).

115. Other national brands have also emphasized the low price per ounce returnable bottle (Strachan, Tr. 2871, 2915–16). Nationally, 65 percent of Dr Pepper's volume is sold in returnable bottles (Clements, Tr. 3994). Eighty-five (85) percent of the volume of the Dr Pepper-Pepsi-Cola Bottling Company in Dyersburg, Tennessee is sold in returnable bottles (Burks, Tr. 3030, 3096). Sixty (60) percent of the volume of Dr Pepper in the State of Texas is sold in returnables (Ippolito, Tr. 3252–53, 3287). In Herminie, Pennsylvania, and Wheeling, West Virginia, the Seven-Up/Royal Crown bottler has approximately 80 percent and 50 percent, respectively, of his sales volume in returnables (Cobetto, Tr. 2818–19, 2837).

116. In July 1971, the average retail price of Coca-Cola in the United States in 16-ounce returnable bottles, according to Neilsen sources, was lower than the average price per ounce at which Coca-Cola in the 6 1/2-ounce returnable bottle was sold at retail in 1900 (Smith, Tr. 716). [48]

117. Neilsen reported that in the period December 1970—January 1971 the retail price per ounce of Coca-Cola in 16-ounce returnable

bottles nationwide was on the average of one percent less than the price per ounce on private label cans sold in chains and large independent food stores (RX 8). In June-July 1971, the nationwide average retail price per ounce for Coca-Cola in 16-ounce returnable bottles was the same as the average price per ounce for private label soft drinks in all containers combined (RX 9).

118. In many local markets, Coca-Cola in 16 and 32-ounce returnable bottles is cheaper than private labels. In Montross, Virginia, a 32-ounce returnable bottle of Coca-Cola in May 1975 retailed for 33 cents; 32 ounces of Rich Food's private label in 28-ounce non-returnable bottles retailed for 38 cents; 32 ounces of Safeway's Cragmont retailed for 48 cents; 32 ounces of A&P's Yukon Club retailed for 53 cents; and 32 ounces of Shasta retailed for 59 cents (Carver, Tr. 1634–35). In Newport News, Virginia, in May 1975, the 16-ounce returnable bottle of Coca-Cola sold at retail for a little over a penny an ounce (six 16-ounce bottles for $1.08 or 96 ounces for $1.08) (Brown, Tr. 1680), while a six-pack of private label soft drinks in cans (72 ounces) retailed for between 99 cents and $1.05, or over 1.33 cents per ounce (Brown, Tr. 1693). In Jamestown, North Dakota, 32-ounce returnable bottles of Coca-Cola retailed at 1.2 cents per ounce and private label cans retailed at 1.4 cents per ounce (Bernabucci, Tr. 1981–82). In San Antonio, Coca-Cola in 16 and 32-ounce returnable bottles retailed at regular everyday prices at about one cent per ounce, whereas private label soft drinks in cans retailed at approximately 18–20 cents each or 1.5 to 1.7 cents per ounce (Alford, Tr. 2492). And in Ada, Oklahoma, 32-ounce returnable bottles of Coca-Cola retailed at 33 cents each or three for a dollar, which is about a penny an ounce (Crabtree, Tr. 2671); 12-ounce cans of private label soft drinks retailed at 18–19 cents each at 1.5 cents per ounce (Crabtree, Tr. 2674); and 64-ounce non-returnable bottles of the private labels retailed at 69 cents or just over one cent per ounce (Crabtree, Tr. 2690). [49]

119. The 16 and 32-ounce returnable bottles provide direct price per ounce competition to private labels (Ellis, Tr. 995, 1021–22; Brown, Tr. 1661; Strachan, Tr. 2870). Because national brands sold in returnables provide the strongest price competition for private labels, food chains dislike handling national brands in economical returnable bottles (Ellis, Tr. 1021–22; Strachan, Tr. 2867A, 2870). In areas where national brands are predominantly in returnable bottles, private label market penetration is weak; in areas where national brands have been forced into non-returnable containers, private labels are strong (Strachan, Tr. 2883–85). In markets where 32-ounce returnables are sold, chains often keep them at locations in the beverage section which are physically distant from their private labels (Burks, Tr. 3032–33).

120. Without exclusive territories the use of the returnable bottle by bottlers of Coca-Cola and other national brands would be substantially reduced, if not eliminated (Smith, Tr. 734–736; Ellis, Tr. 995; Rooks, Tr. 1400, 1431; Bernabucci, Tr. 1994; Roadcap, Tr. 2466; Crabtree, Tr. 2689; Strachan, Tr. 2903; Clements, Tr. 4038–39). If the chain stores converted to a system of warehouse delivery, the chain stores would eliminate returnable bottles entirely because the returnable bottle is incompatible with warehouse delivery (Smith, Tr. 735–36; Ellis, Tr. 995; Rooks, Tr. 1401; Cobetto, Tr. 2838–39; Strachan, Tr. 2870, 2903). In Los Angeles, where national brand soft drinks are delivered to warehouses, no returnable bottles are handled through the warehouse system (Hurst, Tr. 3496).

121. Returnable bottle usage would also decline because bottlers would be reluctant to invest in returnable bottles when they had no assurance that they would be able to recapture their large investment in returnable bottles for reuse (Smith, Tr. 700; Rooks, Tr. 1404; Cobetto, Tr. 2813; Clements, Tr. 4046).

122. If bottlers lose their high volume accounts or such accounts shifted to predominantly nonreturnable containers, the cost of providing returnable bottles to the remaining low-volume accounts will necessarily increase to cover fixed costs (Alford, Tr. 2540; DeLap, Tr. 2590), thereby reducing the price per ounce advantage and economical appeal of returnable bottles to consumers, and consequently reducing demand for returnable packages (Smith, [50] Tr. 735–36; Ellis, Tr. 1020; Roadcap, Tr. 2466; Connellee, Tr. 2989, 2994). Once returnable bottles lose their economy image, and the price per ounce differential with non-returnables narrows, consumers will stop purchasing returnables (Cameron, Tr. 2066–68). Without the economy appeal of the returnable, trippage (*i.e.*, the number of fillings of a returnable bottle) will decline and the returnable bottle will die (Smith, Tr. 734–36).

123. The retail price per ounce differential between Coca-Cola in returnable bottles and non-returnable containers varies in specific markets. For example, in July 1971, in Baltimore it cost the consumer approximatley 30 percent more per ounce to buy Coca-Cola in 16-ounce non-returnable bottles than in 16-ounce returnable bottles and 66 percent more per ounce in 12-ounce cans than in 16-ounce returnable bottles (Ellis, Tr. 982). In Wilmington, Delaware, the retail price of 32-ounce returnable bottles of Coca-Cola is four for $1.69 or 1.32 cents per ounce; the prevailing retail price for cans is six for $1.49 or 2.06 cents per ounce, 36 percent more expensive to the consumer on a per ounce basis (Navarre, Tr. 1541). In May 1975, in Montross, Virginia, the 16-ounce returnable bottle retailed in supermarkets at 1.08 cents per ounce (Brown, Tr. 1680); cans retail at 2 cents per ounce or

approximately twice as much (Brown, Tr. 1680, 1692). In Jamestown, North Dakota, the May 1975 retail price per ounce of Coca-Cola in 32-ounce returnable bottles was 1.2 cents; the price per ounce in 32-ounce non-returnables was 1.5 cents, and in cans, 2.2 cents (Bernabucci, Tr. 1981). In May 1975, Coca-Cola in 16-ounce returnable bottles was on a per ounce basis, 29 percent cheaper than Coca-Cola in 16-ounce non-returnables, 27 percent cheaper than Coca-Cola in 32-ounce non-returnables, 16 percent cheaper than Coca-Cola in 64-ounce non-returnables; and 61 percent cheaper than Coca-Cola in 12-ounce cans in Reading, Pennsylvania (Levin, Tr. 1925). In San Antonio, Texas, the May 1975 retail price per ounce for Coca-Cola in 16 and 32-ounce returnable bottles was about a penny. Coca-Cola in 48 and 64-ounce non-returnable bottles retailed at about 1.5 cents per ounce, or 50 percent more expensive than it is in a 16-ounce returnable bottle, and Coca-Cola in cans retailed at 1.9 cents per ounce, or 90 percent more expensive (Alford, Tr. 2488, 2551).

124. Large size returnable bottles provide the same price per ounce advantages to other national brands as they do to Coca-Cola. Dr Pepper in Dallas sells 16 and 32-ounce returnables at the same price per ounce that prevailed 70 years ago (Clements, Tr. 3994–95). From 1971 until 1974, the Dr Pepper bottler in Dyersburg, Tennessee, was selling Dr Pepper in 16-ounce, and later in 32-ounce, returnable bottles on a per ounce basis at approximately the same price that soft drinks were being sold for in the 1930's (Burks, Tr. 3030). [51]

125. Other brands in large size returnables also sell at a retail price per ounce comparable to private labels. For example, Dr Pepper in 32-ounce returnable/resealable bottles in Dyersburg, Tennessee, in June 1975 retailed for between 41 and 43 cents per bottle (Burks, Tr. 3031). The private label of the largest chain in Dyersburg, Kroger's "Big K," in 28-ounce non-returnable bottles sold for 43 cents in June 1975, or for more than Dr Pepper on a per ounce basis (Burks, Tr. 3032). And in Galveston, Texas, in June 1975, Dr Pepper in 32-ounce returnables was cheaper on a price per ounce basis than private label cans (Ippolito, Tr. 3255–56).

126. Other brands of soft drinks sold in returnable bottles are less expensive on a per ounce basis than the same brands sold in non-returnable bottles and cans. In June 1975, in Galveston, Dr Pepper in 32-ounce returnable/resealable bottles retailed for 33 cents or about one cent per ounce; in 32-ounce non-returnables the price was 49 cents of 1 1/2 cents per ounce; in cans the price was six for $1.40 or almost 2 cents per ounce (Ippolito, Tr. 3255–56). In Dallas, the retail per ounce price of Dr Pepper in cans was 1.75 cents versus less than 1 cent in returnable bottles (Clements, Tr. 3994–96). In Dyersburg, Tennessee, a

32-ounce returnable/resealable bottle of Dr Pepper retailed for between 41 and 43 cents; a 28-ounce non-returnable bottle of Dr Pepper retailed for 49 cents and a six-pack of 12-ounce cans of Dr. Pepper retailed for between $1.37 and $1.39. The retail price per ounce of Dr Pepper in 32-ounce returnable bottles was 1.3 cents, and for cans the per-ounce price was nearly 2 cents (Burks, Tr. 3031–34).

127. Bottlers of Coca-Cola and other brands compete by offering price promotions. Promotions are normally offered in the form of allowances or cents-off the wholesale price per case (Sales, Tr. 1333) or by providing one case free with a given number of cases purchased (Stokes, Tr. 1181–82; Millard, Tr. 2389). Many industry witnesses indicated they [52] compete through price promotions in their respective markets (Ogden, Tr. 840; Sales, Tr. 1237; Navarre, Tr. 1503–05; Carver, Tr. 1604; Christian, Tr. 1854; Filoromo, Tr. 2192–93; Millard, Tr. 2357–58; Alford, Tr. 2510–11; DeLap, Tr 2576–77; Strachan, Tr. 2886; Burks, Tr. 3043, 3088; Hurst, Tr. 3456; Reid, Tr. 3562–63; Clements, Tr. 3995, 4025).

128. Price promotions are increasing substantially year after year (Navarre, Tr. 1503; Bernabucci, Tr. 1986; Millard, Tr. 2357; Strachan, Tr. 2886). For example, the Delaware Coca-Cola Bottling Company in Wilmington, Delaware, has increased its discount or promotional budget, that is the amount of the reduction of normal wholesale prices which it allocates for cents-off promotions, from $70,000 two years ago to $550,000 today (Navarre, Tr. 1503). The Coca-Cola bottler in Jamestown, North Dakota and in LaCrosse, Wisconsin indicated that 10 years ago price promotions were "rarely offered" but that currently his expenditures for promotional allowances ran $50,000 a year in Jamestown and $60,000 in LaCrosse (Bernabucci, Tr. 1986). The bottler of Coca-Cola in Stockton, California, testified that to keep up with competition "we are running into more and more promotions and promotional discounts" (DeLap, Tr. 2576). The amount of money the bottler of Coca-Cola in Stockton spent on cents-off discounts increased from $12,734.42 in 1967 to $104,505.85 in 1974 (DeLap, Tr. 2577). The bottler of Coca-Cola in San Antonio testified that "10 years ago we never did any price promotions" and "now it is a fact of life" and that "if we don't price promote * * * then we are dead" (Alford, Tr. 2508). The Seven-Up bottler in Herminie, Pennsylvania, indicated that he has been "promoting heavily" with cents-off promotions the last four or five years, and that this type of "competition is very keen" (Cobetto, Tr. 2829). [53]

129. Food chains do not always pass on promotions in the form of lower retail prices to the consumer. The bottler of Coca-Cola in Wilmington, Delaware, indicated that the chains pass on the promo-

tions 80–90 percent of the time (Navarre, Tr. 1504). Safeway in Washington, D.C., refused to pass on a 52 cents per case promotion for Coca-Cola during November 1971 and instead increased its margin to 37 percent (Sales, Tr. 1286–87, 1290; RX 23). In November 1974, Dart Drug received a 60 cents per case wholesale price reduction from the Washington, D.C. bottler of Coca-Cola for a two-week period but reduced its retail price to the consumer only during one of the two weeks (Sales, Tr. 1288; RX 24). In Dyersburg, Tennessee, Kroger, the largest food chain in the area, received one case free with the purchase of a case of 32-ounce returnable bottles of Bubble-Up, effectively reducing the wholesale price 50 percent, but did not reduce the price to the consumer below its normal retail price for a carton of 32-ounce returnable resealable bottles (Burks, Tr. 3041–42). In other markets, food chains have refused to pass on promotions to the consumer (Stokes, Tr. 1181–82; Millard, Tr. 2380; Strachan, Tr. 2890; RX 18). During promotions, food chains try to purchase extra stock which they store in their backrooms and then sell at the normal retail price after the promotions (Massey, Tr. 2194; Millard, Tr. 2376). And, in New York City, food chains will not pass on promotions of one case free with ten cases; the bottler of Coca-Cola has to give one case free with five in order to have the wholesale savings passed on (Millard, Tr. 2376–77). The fact that outlets other than food chains receive and pass on promotions influences the food chains' willingness to pass on soft drink promotions (Ellis, Tr. 994, 1021; Sales, Tr. 1319).

130. Promotions for Coca-Cola, Pepsi-Cola, Royal Crown, Seven-Up, Dr Pepper, canned iced teas, and private label flavored carbonated soft drinks affect sales. When bottlers of Coca-Cola are running promotions on Coca-Cola, sales volume increases noticeably (Carver, Tr. 1630–31; Levin, Tr. 1914; Alford, Tr. 2510, 2578). According to bottlers of other brands, promotions of Coca-Cola take sales away from Pepsi-Cola (Strachan, Tr. 2886–87, 2889–90), Seven-Up (Crabtree, Tr. 2682), and Nestea (Hurst, Tr. 3456) and Lipton (Reid, Tr. 3562–63) canned iced teas. When Pepsi-Cola (Stokes, Tr. 1123; Carver, Tr. 1631; Levin, Tr. 1914; Crabtree, Tr. 2682), Royal Crown (Carver, Tr. 1631), Seven-Up (Bernabucci, Tr. 1972; Crabtree, Tr. 2682), [54] Dr Pepper (Alford, Tr. 2510), private labels (Brown, Tr. 1697), Nestea canned iced tea (Hurst, Tr. 3456), and other national brand competitors (Brown, Tr. 1697; Alford, Tr. 2578) run promotions of their own, sales of Coca-Cola are adversely affected: Correspondingly, when Seven-Up (Cobetto, Tr. 2832), Pepsi-Cola (Strachan, Tr. 2886), Nestea (Hurst, Tr. 3456) and other brands run promotions, their sales volume increases.

131. Bottlers of Coca-Cola and other national brands charge a uniform price to both large and small accounts (Smith, Tr. 659;

Navarre, Tr. 1577; Brown, Tr. 1673; Brendle, Tr. 1784; Alford, Tr. 2520; Clements, Tr. 4040, 4060–61). Uniform pricing allows the smaller accounts to be serviced (Smith, Tr. 659; Navarre, Tr. 1577; Alford, Tr. 2520; Clements, Tr. 4042–44).

Competition in Fountain Drinks

132. Coca-Cola and other flavored carbonated soft drinks sold in bottles and cans compete with post-mix soft drink products dispensed at soda fountains and in cup vending machines (Stip. No. 3, CX 1244L, Tr. 481). Bottlers of other national brands face interbrand competition from post-mix Coca-Cola. The interbrand competition among Coca-Cola, Dr Pepper and other post-mix soft drinks has been characterized as "very tough" (Smith, Tr. 672; Clements, Tr. 4017, 4022). Bottlers of Seven-Up and Royal Crown (Cobetto, Tr. 2827–28) and Dr Pepper (Ippolito, Tr. 3262–64) have lost bottle and can accounts to interbrand post-mix competition from "Coca-Cola." Post-mix Dr Pepper has taken bottle and can accounts from "Coca-Cola" (Burks, Tr. 3042–43).

133. Coca-Cola sold by licensed bottlers in bottles, cans and pre-mix containers is subject to vigorous intrabrand competition from post-mix Coca-Cola sold by independent wholesalers. The president of "Coca-Cola" (Smith, Tr. 672, 687, 706–07, 744) and bottlers testified that Coca-Cola sold in bottles, cans and pre-mix containers competes against post-mix Coca-Cola sold by independent wholesalers or jobbers (Ellis, Tr. 990–91; LaDoux, Tr. 1457; Carver, Tr. 1627, 1640; [55] Millard, Tr. 2348–50; Crabtree, Tr. 2677–78). There usually are a number of post-mix wholesalers selling in a given area, including some bottlers of Coca-Cola who also serve as post-mix wholesalers (Sales, Tr. 1257; LaDoux, Tr. 1457).

Competition in Powdered and Noncarbonated Drinks

134. Flavored carbonated soft drinks also face competition from powdered soft drink mixes in pricing, advertising, and shelf space. Price competition from powdered soft drink mixes is evidenced by the low per-ounce price of powdered mix brands (Sales, Tr. 1253). The Coca-Cola Bottling Company of New York analyzed monthly the prices of powdered soft drink mixes in making decisions on the pricing of Coca-Cola and allied products (Millard, Tr. 2322). The surge in sugar costs heightened price competition by increasing the per-ounce price differential between powdered soft drink mixes and sweetened flavored carbonated soft drinks (LaDoux, Tr. 1457). During the summer months media advertising of powdered soft drink mixes intensifies (Carver, Tr. 1639–40). Advertisements stress the lower per-

ounce price of powdered mixes vis-a-vis flavored carbonated soft drinks (Levin, Tr. 1939; Alford, Tr. 2505–06). In 1974, home market sales of powdered soft drink mixes increased substantially while sales of flavored carbonated soft drinks declined (Clements, Tr. 4016–17, 4059–60).

135. Coca-Cola and other national brand flavored carbonated soft drink products also compete to some degree with noncarbonated drinks, such as Hi-C (Sales, Tr. 1257; Strachan, Tr. 2885; Hurst, Tr. 3455), Hawaiian Punch (Rooks, Tr. 1388; Strachan, Tr. 2885; Burks, Tr. 3037), Gatorade (Millard, Tr. 2282), Tru-Ade (Burks, Tr. 2965), fruit juices (Rooks, Tr. 1388; Cobetto, Tr. 2827), and other beverages which satisfy the consumer's desire for liquid refreshment (Smith, Tr. 705; Rooks, Tr. 1389; Alford, Tr. 2483). [56]

136. Flavored carbonated soft drinks "compete with every other liquid a person consumes" (Smith, Tr. 705). There is data which indicates that a human being will consume a finite quantity of liquid over a given period of time (Smith, Tr. 705). Annually, per capita consumption of liquids has remained at about 120 gallons over the last two decades (Hurst, Tr. 3453–54). Within the 120 gallons, there have been fluctuations as consumption of different types of beverages increases and decreases (Hurst, Tr. 3454–55). In this broad sense, Coca-Cola and other flavored carbonated soft drinks compete with every other beverage (Smith, Tr. 705; Navarre, Tr. 1533; Meyers, Tr. 1732; Strachan, Tr. 2861).

Competition in Product Availability

137. Bottlers of Coca-Cola and other national brand flavored carbonated soft drinks compete to have their brands available in a large number of outlets (Sales, Tr. 1344; Navarre, Tr. 1538; Burks, Tr. 3044). This competition was described as "quite vigorous" (Reid, Tr. 3563) and as "constant fighting in the marketplace to make ourselves available" (Ippolito, Tr. 3267). In the soft drink industry, "[i]t seems like everyone would like to be everywhere, on every street corner * * *." (Reid, Tr. 3563.)

138. To provide availability, bottlers of Coca-Cola and other national brands have not imposed minimum delivery requirements. Some deliver one case of product on a weekly basis (Sales, Tr. 1232; Christian, Tr. 1869; Filoromo, Tr. 2191–92; Millard, Tr. 2374; Burks, Tr. 3013). This contrasts with warehouse delivered soft drink products, such as Shasta, which has minimum delivery requirements at its Baltimore, Maryland, and Union, New Jersey, plants of 500 cases of 12-ounce cans and 660 and 550 cases, respectively, of 28-ounce non-returnable bottles (CX 1262). [57]

139. Bottlers of different brands compete to place vending machines (Sales, Tr. 1333; Brendle, Tr. 1781–82; Christian, Tr. 1852–53; Ippolito, Tr. 3267; Clements, Tr. 4026). The president of the Dr Pepper Company testified that competition for vending machine locations is a "very, very intensive battle all the time" because the bottler makes an extreme effort to obtain a prime location but has no assurance that he is going to be able to hold that location from some competitor (Clements, Tr. 4026). In Washington, D.C., the bottler of Coca-Cola competes with Pepsi-Cola by placing vending machines in unproductive outlets as part of its image building process (Sales, Tr. 1333).

140. Bottlers also compete to supply soft drinks and services at special events (*e.g.*, school picnics, football games, etc.) in order to create consumer demand through sampling of the soft drink product, as well as to build goodwill (Stokes, Tr. 1078; LaDoux, Tr. 1460; Levin, Tr. 1916; DeLap, Tr. 2583; Strachan, Tr. 2895; Burks, Tr. 3018–19; Clements, Tr. 3992–93).

Competition in Merchandising

141. Effective merchandising of soft drinks requires adequate shelf space in food stores. The president of the Dr Pepper Company testified that shelf space determines "whether you live or die" in a retail account (Clements, Tr. 4000). Bottlers testified that adequate shelf space is "a means of survival" (Sheldon, Tr. 2620); "probably one of the biggest keys to sales success in a supermarket" (Burks, Tr. 3019–20); "critical" (LaDoux, Tr. 1465); and a "constant problem" (Alford, Tr. 2513). L. T. Christian summarized the relationship between shelf space and sales when he testified that "[t]he larger the shelf space, the more sales I will make" (Tr. 1858).

142. Bottlers compete in home market accounts, *e.g.*, food stores, to obtain shelf and display space. They also compete in the placement of point-of-sale advertising, stock rotation, and in providing frequent service (Millard, Tr. 2324–25). [58]

143. Competition for shelf space in food stores was described as follows: "[b]loody, fierce, makes the Battle of the Bulge look like a Sunday school picnic" (Navarre, Tr. 1536); "every day battle," (LaDoux, Tr. 1459); "ferocious" (Ippolito, Tr. 3266); "intensive" (Ogden, Tr. 840); "constant day in and day out battle" (Millard, Tr. 2325). In discussing all forms of competition among soft drink products, the president of the Dr Pepper Company described shelf space competition as "probably one of the toughest ones" (Clements, Tr. 4025). To obtain more and better shelf space, bottlers of Coca-Cola conduct "space to sales" studies for food stores to persuade food store management to allocate more space to their respective products

(Navarre, Tr. 1540). Point-of-sale material is provided to customers free of charge (Levin, Tr. 1915), and is placed by route salesmen who periodically check the material (Rooks, Tr. 1372).

144. Bottlers also compete to place carton coolers in food stores, and to set up special racks or gondolas which help sales of their respective products (Ogden, Tr. 840; Rooks, Tr. 1363; Millard, Tr. 2325; Strachan, Tr. 2892). Displays increase sales substantially (Sales, Tr. 1221; Reid, Tr. 3556–57; Clements, Tr. 4001). Bottlers also compete by providing refrigeration units free or at a nominal charge in which to store soft drinks in cartons. They are called visi-coolers or carton coolers and cost $600 to $1100 each (DeLap, Tr. 2574–75; Strachan, Tr. 2868; Connellee, Tr. 2968–69).

Competition in Providing Service

145. Another important aspect of merchandising competition among soft drink bottlers is in service they provide resellers (Sales, Tr. 1267; Brown, Tr. 1682–83; Levin, Tr. 1915; Ippolito, Tr. 3244). Competition in the area of service was described as "the name of the game" (LaDoux, Tr. 1464), and "a key to success" (Burks, Tr. 3008). The president of The Coca-Cola Bottling Company [59] of New York, Inc., indicated the soft drink industry "was enormously dependent" on frequency of service (Millard, Tr. 2319). As one bottler of Coca-Cola stated, "[i]f we fall down on service in supermarkets, Pepsi starts getting the business from us and vice versa. It is a very competitive business" (Brown, Tr. 1682–83).

146. Service competition embraces a number of separate competitive elements. First, service competition involves frequency of service in delivery of product by a route salesman. Frequency of service is necessary because, on a container basis, soft drinks are the fastest moving item in a food store (Hurst, Tr. 3511). Supermarkets and other accounts are frequently served more than one time per week (Crabtree, Tr. 2664; Ippolito, Tr. 3242–43; Hurst, 3465–66; Reid, Tr. 3567). Bottlers frequently provide service to food chains on weekends, including Sundays (Crabtree, Tr. 2664; Strachan, Tr. 2892).

147. Service competition also emphasizes such tasks as cleaning and filling beverage coolers and sorting empty bottles (Christian, Tr. 1856; Levin, Tr. 1915; DeLap, Tr. 2581; Burks, Tr. 3008–09).

148. Bottlers also engage in service competition with respect to keeping vending machines supplied with soft drinks and in providing prompt, usually free, repairs for vending machines which become inoperative (Smith, Tr. 697; Carver, Tr. 1633; Levin, Tr. 1915; Connellee, Tr. 2968). Some bottlers, such as the bottler of Coca-Cola in

Stockton, California, provide 24-hour-a-day repair service even on weekends and holidays (DeLap, Tr. 2581). [60]

Competition in Packaging

149. Soft drink bottlers compete in packaging (Ellis, Tr. 986–89, 1054–55; Carver, Tr. 1631; Levin, Tr. 1913–14; Roadcap, Tr. 2427; DeLap, Tr. 2580; Crabtree, Tr. 2681; Cobetto, Tr. 2829–30; Ippolito, Tr. 3266; Clements, Tr. 4025).

150. Pressure from competitive packages forced The Coca-Cola Company in 1955 to abandon its single package (the 6 1/2-ounce returnable bottle) philosophy and add other packages (Smith, Tr. 714). Today, Coca-Cola in the United States is being sold in 42 different package types, sizes, and configurations (*e.g.*, 6-packs, 8-packs) (Ellis, Tr. 1054). No bottler of Coca-Cola sells all packages (Ellis, Tr. 1054). The local competitive situation varies immensely and it primarily determines which packages, sizes, and configurations are used by a particular bottler of Coca-Cola (Ellis, Tr. 1054; Roadcap, Tr. 2427). For example, in South Carolina, because of a state tax bottlers use 36-ounce rather than 32-ounce returnable bottles to offer the best price to the consumer (Ellis, Tr. 1055).

151. Each national brand soft drink bottler must offer a wide variety of packages in order to compete (DeLap, Tr. 2580). For example, The Coca-Cola Bottling Company of New York, Inc., produces and sells a total of 82 package sizes and types (Millard, Tr. 2320). The bottler of Coca-Cola in San Antonio testified that "we will not be out-packaged" (Alford, Tr. 2483), and that he responded to the introduction of 64-ounce non-returnable bottles of Pepsi-Cola in his territory by obtaining two weeks later 64-ounce non-returnable bottles of Coca-Cola from the bottler of Coca-Cola 600 miles away in Las Cruces, New Mexico. He continued to transport 64-ounce non-returnables 600 miles and sell them at the same price as Pepsi-Cola, at no profit, for a period of four months until he was able to obtain equipment to produce that package size (Alford, Tr. 2483–84, 2511–12). [61]

152. Pepsi-Cola recently took two percent of the home market volume away from Coca-Cola in Ada, Oklahoma by offering a package—the 64-ounce returnable bottle—which the bottler of Coca-Cola did not have available (Crabtree, Tr. 2681–82). The Havre de Grace Pepsi bottler called package competition from Coca-Cola "brutal" (Connellee, Tr. 2965–66). Within two weeks after he introduced a 16-ounce returnable/resealable bottle in Havre de Grace, the Coca-Cola bottler introduced it in that size (Connellee, Tr. 2966).

153. The Dr Pepper bottler in Galveston indicated there was so

much packaging competition that "[w]e have got a packaging revolution going on right now in the [soft] drink business" (Ippolito, Tr. 3266). The Dr Pepper bottler in Dyersburg, Tennessee, whose territory embraces parts of the territories of four bottlers of Coca-Cola, testified that three of his competitors had 32-ounce returnable bottles of Coca-Cola on the market within two weeks after he introduced the package (Burks, Tr. 3046).

Competition with New Entries

154. Over the last two decades, there has been vigorous and increasing competition from the entry of new types and brands of soft drink products (Stip. No. 3, CX 1244H–1244I, Tr. 477–78; Brendle, Tr. 1781; Roadcap, Tr. 2450). After losing market position, The Coca-Cola Company was forced to abandon its single product philosophy around 1960 and to introduce a line of flavors and various allied products (Smith, Tr. 714–15). [62]

155. A number of entirely new types of soft drink products have entered the market, including low-calorie soft drinks (Stip. No. 3, CX 1244H, Tr. 477). Low-calorie drinks compete with sugar sweetened soft drinks (Millard, Tr. 2359–60). Although No-Cal and Diet-Rite were originally marketed in 1953, diet flavored soft drinks did not become a significant market factor until the early 1960's. Following the cyclamate ban in October 1969, which virtually removed low-calorie soft drinks from the market, soft drink companies began marketing saccharin substitutes which by the end of 1970 accounted for about 10 percent of total soft drink sales (Stip. No. 3, CX 1244I; Tr. 477). Substantial numbers of low-calorie flavored carbonated soft drinks are being marketed today, including TAB (Smith, Tr. 585), diet TAB flavors (Smith, Tr. 644), Fresca (Smith, Tr. 585), diet-Pepsi (Brown, Tr. 1684), diet Royal Crown, Diet-Rite (Stokes, Tr. 1146), No-Cal (Stokes, Tr. 1146), Weight Watchers (Levin, Tr. 1899), diet Shasta (Meyers, Tr. 1714–15), Sugar Free Dr Pepper (Millard, Tr. 2344), diet Seven-Up (Millard, Tr. 2344), Nestea sugar free canned iced tea (Hurst, Tr. 3450), large numbers of low-calorie private labels (Hornsby, Tr. 3158–59), and others.

156. Another new category of soft drinks which has been introduced in the last decade is the "isotonic" or "thirst quenching" soft drink, such as Gatorade (Stip. No. 3, CX 1244I; Tr. 477).

157. Yet another new type of soft drink is the iced tea sold by bottlers in cans (Hurst, Tr. 3451, 3478–79) and bottles (Hurst, Tr. 3525–26). Iced tea flavored soft drinks are manufactured by bottlers (Hurst, Tr. 3474, 3478–79), distributed by bottlers (Hurst, Tr. 3477), and sold in the carbonated beverage section of supermarkets (Hurst, Tr. 3456;

Reid, Tr. 3553–54, 3604) and in soft drink vending machines (Burks, Tr. 3007; Reid, Tr. 3563). Tea was first test marketed in cans in 1968 (Hurst, Tr. 3458). [63]

158. Entry of new firms and brands into the soft drink industry is easy. There are numerous flavor houses from which a company entering the soft drink business can purchase syrups or concentrates (Meyers, Tr. 1734). There are also a large number of facilities available for the manufacture of soft drinks in bottles and cans which can be purchased, leased, or which will produce flavored carbonated soft drinks on a contract basis (Meyers, Tr. 1734; Hornsby, Tr. 3148). Competition among contract bottlers or canners is very tough (Hornsby, Tr. 3148, 3159–60, 3179). There is no problem in obtaining an adequate supply of cans or bottles in which to package a new brand of soft drinks (Meyers, Tr. 1734). Personnel with experience are available in the industry (Meyers, Tr. 1734). Many new companies have entered the packaged soft drink business in the last 10 years, such as A&W Root Beer (Meyers, Tr. 1735; Connellee, Tr. 2964).

159. Many brands of soft drinks have been able to enter new markets and obtain immediate distribution in such markets at virtually no expense by entering into exclusive territorial license agreements with established bottlers already manufacturing and distributing other national brand soft drinks (Clements, Tr. 4063). By this "piggybacking" on the products of an established national brand bottler, a brand attempting to enter a market capitalizes on the bottler's existing production facilities, vehicles, vending machines, sales force, and good will in a market and can obtain substantial distribution in a market in a very short time (Bernabucci, Tr. 2005; Millard, Tr. 2338–40; Clements, Tr. 4063).

160. By entering into exclusive territorial license agreements with established national brand bottlers and expanding the number of its bottlers from 395 in 1961 to 512 in 1971, Dr Pepper Co. has been able to enter a substantial number of new markets and expand the geographic areas in which Dr Pepper is available from those containing 114 million people to areas with 198 million people or almost 98 percent of the population (Clements, Tr. 3983, 3986–87). During this period, Dr Pepper's national share of the flavored carbonated soft drink market grew from 2 to 2 1/2 percent to nearly 4 percent, and is about 5 percent today (Clements, Tr. 3981). In 1971, about 70 percent of the bottlers of Dr Pepper were licensed to sell other brands (Clements, Tr. [64] 3983–84). During the 1961 to 1971 period, 70 percent of Dr Pepper's growth came from the multibrand plants (Clements, Tr. 3985), and Dr Pepper grew at a rate 2 to 3 times the rate of the industry (Clements, Tr. 3981).

161. Similarly, Nestea canned iced tea was able to obtain distribution in areas serving approximately 90 percent of the population (Hurst, Tr. 3483) in three years by entering into exclusive territorial licenses (Hurst, Tr. 3473–74) with 135 established national brand bottlers, including 55 to 60 bottlers of Pepsi-Cola, 45 to 50 bottlers of Seven-Up, and 30 bottlers of Coca-Cola (Hurst, Tr. 3477–78). In three years of licensing bottlers, Nestea has attained this distribution with the commitment of less than 20 employees (Hurst, Tr. 3484) and no investment in capital equipment (Hurst, Tr. 3484–85). In the same way, Lipton canned iced tea was also able to obtain distribution in areas serving 90 percent of the population within a period of four years (Reid, Tr. 3570–71) by entering into exclusive licenses with about 200 established national brand bottlers of Coca-Cola, Pepsi-Cola, Seven-Up and Royal Crown (Reid, Tr. 3574). Lipton was able to obtain this distribution with the commitment of only six people on a full-time basis (Reid, Tr. 3574) and no capital investment in land, production facilities, transportation vehicles or packaging supplies (Reid, Tr. 3572–73).

162. Other new brands, such as Welch's Sparkling Grape Soda, which "piggybacked" into the New York area by affiliating with The Coca-Cola Bottling Company of New York (Millard, Tr. 2342–43; RX 50A–50X), Bubble-Up, which entered into exclusive territorial license agreements with bottlers including the Dr Pepper bottler of Dyersburg Tennessee (Burks, Tr. 3006–07; RX 100A–100F); Frostie root beer (RX 93A–93C; RX 115A–115C); Mason's Root Beer (RX 105A–105F); NuGrape (RX 116A–116D); and Suncrest (RX 117A–117D) have similarly been able to enter new local markets. [65]

Market Shares

163. On a unit basis, sales of Coca-Cola as a percentage of total domestic food store sales of flavored carbonated soft drinks are estimated by Neilsen, the source generally relied on by the soft drink industry (Stip. No. 5, RX 2D), to have declined from 41.2 percent of total domestic food store sales of flavored carbonated soft drinks in 1950 to 24.4 percent in 1965 (Stip. No. 5, RX 2C). During that same period, sales of Pepsi-Cola increased from 15.5 percent in 1950 to 23.9 percent in 1960 and then declined to 19.3 percent in 1965 (Stip. No. 5, RX 2P). In 1950, the percentage of total domestic food store sales of flavored carbonated soft drinks accounted for by Royal Crown was 5.1 percent; by 1965, the percentage had declined to 4.8 percent (Stip. No. 5, RX 2U). During the period from 1950 to 1965, the percentage of total domestic food store sales accounted for by Seven-Up ranged from 5.8

percent in 1950 to 10.9 percent in 1960 and back to 7.8 percent in 1965 (Stip. No. 5, RX 2S).

164. Beginning in 1955, Neilsen began to report data on a statistical case basis, which converts soft drinks sold to the equivalent of 24 8-ounce containers (Stip. No. 5, RX 2B). On a statistical case basis, between 1960 and 1971 the percentage of total domestic food store sales of flavored carbonated soft drinks accounted for by Coca-Cola declined from 22.3 percent to 20.8 percent (Stip. No. 5, RX 2C). During the same period, sales of Pepsi-Cola decreased from 24.6 percent to 19.3 percent (Stip. No. 5, RX 2P). The regional market share for Coca-Cola also fluctuated substantially over a period of time (Stip. No. 5, RX 2D–2E).

165. The importance of any particular package sold through food stores varies from bottler to bottler and from region to region. The sales of Coca-Cola as a percentage of total sales of that package also vary from bottler to bottler and region to region. During October and November 1971, for example, cans ranged from 18.0 percent of the physical case sales of flavored carbonated soft drinks in food stores in "Coca-Cola's" Region 7 (Southeast U.S.) to 42.2 percent in Region 2 (metro New York area). **[66]** Sales of Coca-Cola as a percentage of total physical case sales of carbonated soft drinks in cans ranged from a low of 6.9 percent in Region 5 (metro Chicago area) to a high of 20.2 percent in Region 8 (Southwest U.S.) (Stip. No. 5, RX 2I). The same variations occur for non-returnable and returnable bottles (Stip. No. 5, RX 2J–2K).

166. The largest selling brands of flavored carbonated soft drinks sold in various markets change over relatively brief periods of time. During the period from 1969 to 1974, Coca-Cola and Pepsi-Cola were both at times the leading brand in Detroit, Pontiac, Lansing, Flint, and Wyandotte, Michigan; Las Vegas, Nevada; Kansas City, Missouri; Milwaukee, and Green Bay, Wisconsin; and Waterbury, Connecticut. Coca-Cola and Seven-Up were at different times the leading brand in Seattle, Washington. Pepsi-Cola, Coca-Cola and Seven-Up were at different times the leading brand in Portland, Oregon (Stip. No. 5, RX 2Z2–2Z38).

Environmental Considerations – Returnable v. Non-Returnable

167. From the standpoint of raw materials consumed in the manufacture of soft drink containers; the energy used in the processing of raw materials, the manufacture of containers, the filling of containers, and the transportation associated therewith; water use; solid waste generation; air pollutants; water-borne wastes; and energy effluents, the returnable bottle is the preferred soft drink container

even at trippage rates below ten (Nuss, Tr. 3799–3802; RX 126Q; RX 127F–127K). At approximately four trips, the returnable bottle has the same composite impact on the environment as the conventional steel can (Nuss, Tr. 3801; RX 126Z20–126Z23). A returnable bottle with trippage as low as two still has roughly the same impact as a nonreturnable bottle (Nuss, Tr. 3801; RX 126Z20–126Z23). A returnable bottle with a trippage between four and five has the same composite environmental impact as does an aluminum can which is recycled at an 80 percent rate (Nuss, Tr. 3802; RX 126Z20–126Z23). [67]

168. Nationally, on the basis of 1974 data, the average trippage of returnable bottles of Coca-Cola is approximately 14 (Teasley, Tr. 3645).

The Effect of Eliminating Exclusive Territories

169. If territorial exclusivity were eliminated, the chain stores would request bids for warehouse delivery from bottlers with the equipment and capacity to service their needs, thus resulting in short-term wholesale price competition for warehouse delivery business (Smith, Tr. 659, 729–30, 739; Ellis, Tr. 991–93; Stokes, Tr. 1152–53; Navarre, Tr. 1568; Levin, Tr. 1929; Bernabucci, Tr. 1988-89; Millard, Tr. 2375; Roadcap, Tr. 2464–66).

170. A short-term or temporary wholesale price reduction might result from wholesale price competition for warehouse delivery of nonreturnable containers, but only long enough to force the small bottlers out of business and reduce competition (Smith, Tr. 659; Stokes, Tr. 1151–52; Navarre, Tr. 1571; Levin, Tr. 1936; Strachan, Tr. 2900; Hurst, Tr. 3502).

171. Even with lower wholesale prices for soft drinks, there is no assurance that the chain stores would pass this reduction on to the consumer in the form of lower retail prices (Smith, Tr. 739; Ellis, Tr. 1001–02, 1022; Stokes, Tr. 1153; Sales, Tr. 1286; Navarre, Tr. 1571–72; Millard, Tr. 2377; Alford, Tr. 2525–27, 2543; Strachan, Tr. 2899; Hurst, Tr. 3488–89; Clements, Tr. 4040; RX 23, RX 24). The president of The Coca-Cola Company testified that it was "speculative" to predict lower retail prices will result from lower wholesale prices (Smith, Tr. 731, 739, 740). In the early 1960's, during an experiment with warehouse delivery of cans by bottlers of Coca-Cola in the San Francisco area to Safeway, Lucky, and Purity, Coca-Cola and Pepsi-Cola retailed at the same price in chain stores irrespective of the fact that the wholesale price for Coca-Cola in cans delivered to the warehouse was lower than the price of Pepsi-Cola in cans delivered directly to retail stores (DeLap, Tr. 2572; Sheldon, Tr. 2626, 2631). In another instance, Alpha Beta chain stores in parts of California in May 1975, received Coca-Cola in cans through a Los Angeles [68] warehouse, but there was no retail

price difference between warehouse delivered Coca-Cola in cans and store-door delivered canned Pepsi-Cola (DeLap, Tr. 2585; Sheldon, Tr. 2632–34). Also, there was no difference between the retail price for Coca-Cola in cans in Alpha-Beta Stores and the price for stores receiving Coca-Cola in cans by route delivery (DeLap, Tr. 2589).

172. In June 1975, Delaware Punch and Dad's Root Beer were delivered to a Houston warehouse and sold in supermarkets in Galveston, Texas (Ippolito, Tr. 3239–41). Despite a lower wholesale price, which for Delaware Punch was approximately 90 cents per case lower (Ippolito, Tr. 3242), these products were priced by the chain stores at the same retail price as the store-door delivered national brands such as Coca-Cola and Pepsi-Cola (Ippolito, Tr. 3241). The Dr Pepper Company was forced by the chain stores to reduce the wholesale price of Dr Pepper by a minimum of $.50 before the chain stores would accept Dr Pepper for warehouse delivery in Los Angeles. Nevertheless, Dr Pepper was sold in chain stores at the same retail price as store-door delivered Coca-Cola (Clements, Tr. 3997–98, 4046–47).

173. Chains take lower margins on private label soft drinks to maintain the price differential between private labels and national brands and to thereby indicate to consumers that all of their private label products are cheaper than national brand products (Alford, Tr. 2527). With respect to food products generally, including products delivered through chain warehouses, the National Commission on Food Marketing found that the advertised brand retail price was about 20 percent higher than the private label product with which it competed (RX 106F). For example, food chains keep a 30 percent differential between Minute Maid frozen concentrate orange juice and their private labels to establish the "bargain" value of their private labels (Smith, Tr. 730–31). And, in Baltimore, chains refused to sell Coca-Cola in flat-top cans on a loose pack basis because the low price [69] would cut into their private label business (Ellis, Tr. 1001–02). Even with lower wholesale prices for Coca-Cola and other national brand soft drinks delivered to warehouses, chain supermarkets are not likely to reduce their retail prices for national brands because of their usual practice of maintaining the price spread between their private label brands and national soft drink brands (Smith, Tr. 730–31; Ellis, Tr. 1001–03; Navarre, Tr. 1571–72).

174. With the elimination of exclusive territories and a switch from store-door to warehouse delivery to chain supermarkets, bottlers of Coca-Cola products and of other brands of soft drinks would be unable to engage in effective merchandising activities and merchandising functions would be substantially curtailed or eliminated (Ellis, Tr.

1005; Sales, Tr. 1317–18; LaDoux, Tr. 1474; Christian, Tr. 1864; Bernabucci, Tr. 1992; Strachan, Tr. 2901; Connellee, Tr. 2982).

175. Bottlers of Coca-Cola charge the same price to all their customers; but if bottlers lost chain store outlets which are the high volume and high profit accounts to warehouse delivery, they would be obliged to cut back service to small accounts or to raise prices, either of which would reduce volume (Smith, Tr. 659–60, 736).

176. Without exclusive territories, the price of soft drink products would have to increase in the smaller non-chain store accounts still serviced by bottlers (Smith, Tr. 659, 736; Stokes, Tr. 1152; Levin, Tr. 1929; Filoromo, Tr. 2187–88; Sheldon, Tr. 2637; Connellee, Tr. 2980; Hurst, Tr. 3500–01; Clements, Tr. 4036).

177. Without exclusive territories, bottlers would reduce the frequency of service to those small outlets which they continued to serve (Ellis, Tr. 1000, 1003–04; Rooks, Tr. 1401; Brendle, Tr. 1784; Bernabucci, Tr. 1991–92; Alford, Tr. 2520; Ippolito, Tr. 3272).

178. Without exclusive territories other small accounts would not be served at all (Stokes, Tr. 1077–78, 1152; Sales, Tr. 1278–79; LaDoux, Tr. 1473; Levin, Tr. 1932–34; Filoromo, Tr. 2188; Alford, Tr. 2520–21; Burks, Tr. 3054–55; Clements, Tr. 4038, 4074–77) because the higher incremental cost of servicing those accounts by route trucks would be prohibitive without the large volume outlets lost to warehouse delivery (Smith, Tr. 659–60; Rooks, Tr. 1404–05; Filoromo, Tr. 2188; Clements, Tr. 4036). [70]

179. Without exclusive territories, a substantial number of soft drink brands and flavors would be eliminated in local markets (Smith, Tr. 730–32; Sales, Tr. 1282, 1317–18; Navarre, Tr. 1550–51; Brendle, Tr. 1785; Levin, Tr. 1932–33; Hurst, Tr. 3491, 3503; Clements, Tr. 4048–50).

180. The chains already want fewer brands and flavors and would cut out slower moving brands if they had warehouse delivery and could better determine a brand's sales (Ellis, Tr. 1007; Navarre, Tr. 1550–51; Clements, Tr. 4048–50). Many chains have refused to handle slower moving products such as TAB flavors in New York (Millard, Tr. 2377–78); Crass flavors in Washington (Sales, Tr. 1232); Suncrest and NuGrape in Galveston (Ippolito, Tr. 3259); and K–S Canning Company's own brands (Hornsby, Tr. 3169–70). The Kroger chain in Dyersburg, Tennessee (Ippolito, Tr. 3256–57) and the Handy Andy chain in San Antonio (Alford, Tr. 2542) both threw out Shasta when they introduced their own private labels. As many national brand bottlers go out of business, the lesser known secondary brands which had "piggybacked" into local markets by licensing such bottlers would be forced out of local markets (Hurst, Tr. 3490–91). Moreover, many bottlers seeking to survive in a warehouse delivery environment would

cut their slower moving brands (Millard, Tr. 2370–71; Reid, Tr. 3582; Clements, Tr. 4048).

181. Even better known brands such as Seven-Up and Dr Pepper might not survive in many local markets (Sales, Tr. 1220, 1317; Navarre, Tr. 1550–51). Smaller trademark licensors, such as the Dr Pepper Company (Clements, Tr. 4048–50) and Thomas J. Lipton Co. (Hurst, Tr. 3491) would be placed in economic peril as availability of their products in many markets was reduced or eliminated entirely. The Nestle Company, for example, estimates that 60 percent of the Nestea bottlers would go out of business without exclusive territories for national brands (Hurst, Tr. 3500). Many of the weaker allied products of large licensors, such as The Coca-Cola Company's Fanta (Hurst, Tr. 3491–92) and Fresca (Smith, Tr. 610), would also be forced out of local markets (Hurst, Tr. 3491–92).

182. The long term result of eliminating territories would be that the strongest three or four national brands in each local market and private labels would survive (Sales, Tr. 1220) and ease of entry would diminish. The president of Dr Pepper Company said with respect to entry into new local markets "no one else will ever do it again" (Clements, Tr. 4050–51). [71]

183. Nationally hundreds of bottlers of Coca-Cola and other brands would go out of business if exclusive territories were determined to be unlawful (Smith, Tr. 615, 732–33; Clements, Tr. 4037–38). The number of bottlers would be reduced to a fraction of the number that would otherwise exist under the present system (Smith, Tr. 615). Small bottlers of Coca-Cola and other national brands testified that they would go out of business in a short period of time if territorial exclusivity were declared illegal (Rooks, Tr. 1399–1402, 1405–06, 1412, 1418–19; LaDoux, Tr. 1472; Carver, Tr. 1551, 1637–38; Brown, Tr. 1699–1700; Brendle, Tr. 1782–84; Christian, Tr. 1863, 1865–66, 1873, 1876; Levin, Tr. 1928–29; Bernabucci, Tr. 1992–93, 1995; Cameron, Tr. 2074, 2098–99; Filoromo, Tr. 2185–86; Massey, Tr. 2238; Roadcap, Tr. 2457–60).

184. Large bottlers and other witnesses agreed that such small bottlers and some large bottlers would be forced out of business if territories were declared illegal (Smith, Tr. 614–15, 732–34, 807–08; Ellis, Tr. 1008–09, 1011, 1041, 1045; Sales, Tr. 1284, 1317; Navarre, Tr. 1570–71; Alford, Tr. 2515, 2517–19; Hurst, Tr. 3490, 3499–3500; Reid, Tr. 3581–82; Clements Tr. 4035–38, 4048–50). The fate of the small bottler was variously described as "doomed," "would go down the drain," (Sales, Tr. 1284, 1317); "simply be a matter of time," "completely out of business" (Rooks, Tr. 1402, 1412); "disappear rather immediately" (Navarre, Tr. 1551); "total disaster" (Brendle, Tr. 1782);

"disastrous" (Sheldon, Tr. 2636); "doomsday" (Connellee, Tr. 2976); "doomed," "just a matter of time" (Burks, Tr. 3048).

185. Without exclusive territories, large bottlers of Coca-Cola and other national brands would take small bottlers' chain store business because chain store warehouses are located mainly in territories of large bottlers (Rooks, Tr. 1399; LaDoux, Tr. 1472; Brendle, Tr. 1782–84; Levin, Tr. 1928–29; Filoromo, Tr. 2186–2187; Massey Tr. 2238; Roadcap, Tr. 2458–60; DeLap, Tr. 2590; Sheldon, Tr. 2636; Crabtree, Tr. 2684; Burks, Tr. 3092–93; Clements, Tr. 4036). The loss of the chain store accounts, [72] comprising so large a part of the bottler's volume, would put small bottlers out of business (Smith, Tr. 732–33; LaDoux, Tr. 1472; Brendle, Tr. 1782–1783; Christian, Tr. 1873; Levin, Tr. 1929; Bernabucci, Tr. 1992–93; Filoromo, Tr. 2186–87; Alford, Tr. 2517–18). Because soft drinks are a high volume, low mark-up product, volume is critical. For example, the bottler of Coca-Cola in San Antonio made a study that showed that a loss of 15–20 percent of its volume would put it at a break-even point due to its fixed costs (Alford, Tr. 2518).

186. Small bottlers of Coca-Cola are located close to large bottlers. For example, the Westminster, Maryland bottler, surrounded by bottlers of Coca-Cola in Washington, D.C., Baltimore, Maryland, and Wilmington, Delaware, testified that "[i]t is sort of like the flea and the elephant" (Roadcap, Tr. 2459). This situation applies to many small bottlers of Coca-Cola. For example, there are at least six large bottlers of Coca-Cola within 150 miles of the Hartwell, Georgia bottler of Coca-Cola (Rooks, Tr. 1359–60). The Spirit Lake, Iowa bottler is located within 90–120 miles of the Des Moines, Iowa bottler of Coca-Cola as well as within 90–120 miles of a plant owned by the Minneapolis bottler of Coca-Cola (LaDoux, Tr. 1448–49). The Annapolis bottler of Coca-Cola is surrounded by the Baltimore territory on one side and the Washington territory on the other side (Brendle, Tr. 1773). The bottler of Coca-Cola in LaCrosse, Wisconsin is surrounded on three sides by large bottlers with their own canning lines (Bernabucci, Tr. 1976–77). The bottler of Coca-Cola in Coatesville, Pennsylvania is located near the Philadelphia bottler owned by Associated Coca-Cola Bottling Company and "within arm's reach" of the bottler in Baltimore (Filoromo, Tr. 2185). Family-owned bottlers of Coca-Cola within 75 miles of The Coca-Cola Bottling Company of New York, Inc., include Pittston, Pottsville, Reading, Coatesville, Williamsport, York, and Lancaster, Pennsylvania, and North Hampton and Pittsfield, Massachusetts (Millard, Tr. 2362). There are 13 bottlers of Coca-Cola with annual case sales ranging from 100,000 to 700,000, located within 150 miles of the Coca-Cola Bottling Company of San Antonio, Texas, which had case sales of 5,500,000 in 1974 (Alford, Tr. 2480, 2514). The Coca-

Cola Bottling Company of the [73] Peninsula is completely surrounded by the Coca-Cola Bottling Company of California (Sheldon, Tr. 2636). The bottler of Coca-Cola in Ada, Oklahoma is within 120 miles of the large bottler of Coca-Cola in Tulsa and 32 miles from a distribution center of the Oklahoma City bottler of Coca-Cola (Crabtree, Tr. 2683).

187. Some large bottlers, because of their proximity to food chain warehouses and because of their greater financial resources, would be in a financial position to underprice small bottlers for a short period on cans and non-returnable bottles, and thereby take away enough of the small bottler's volume to put him out of business (Ellis, Tr. 1018–19; Carver, Tr. 1613, 1637–38; Levin, Tr. 1936–38; Bernabucci, Tr. 1988; Filoromo, Tr. 2185–87; Roadcap, Tr. 2458–59; Alford, Tr. 2515; Connellee, Tr. 2976–78; Burks, Tr. 3052, 3091–93; Ippolito, Tr. 3275; Reid, Tr. 3582).

188. A small bottler could not supply chain store warehouses by allowing "backhauling" (*i.e.*, the buyer takes delivery at the supplier's point of shipment) from his bottling plant, because the chain store truck servicing the few stores in that territory would not have enough room to pick up a significant supply on a backhaul (Rooks, Tr. 1417; Christian, Tr. 1843; Roadcap, Tr. 2458–59). An empty tractor-trailer can only accommodate 2,000 cases of 12-ounce cans (Meyers, Tr. 3175). Large bottlers could still deliver to a nearby chain warehouse at a lower cost than the chain transport could pick up on a backhaul. As the former president of the Coca-Cola Bottling Company of Baltimore testified: "It is not free to take a great big transport into a bottling plant in Westminster, pull up to their dock, wait to be loaded, you know, loaded on the dock, and the time that is wasted there, it is not free. I am quite sure that we could deliver from Baltimore to the A&P warehouse cheaper than they could pick up from Westminster on their trucks and deliver. And I think that will be the deciding factor." (Ellis, Tr. 1015.) [74]

189. Because price is the determining factor in selling to the chains, and because the per case cost of delivering a transport full of Coca-Cola from a plant in Baltimore to a chain store warehouse would only be 2–3 cents a case, the Baltimore plant could take away chain business from any bottler allowing plant pick-up simply by dropping the per case price by a nickle (Ellis, Tr. 1018–19).

190. Small bottlers could not survive by merging their plants with other small bottlers or by entering into cooperative arrangements (Ellis, Tr. 1045–46; Rooks, Tr. 1418–19; Navarre, Tr. 1570–71; Levin, Tr. 1938–39; Filoromo, Tr. 2139–41, 2214; Roadcap, Tr. 2467). All that would result is "just a bunch of small bottling plants together that will all go out of business" (Ellis, Tr. 1045) and thereby obtaining a "larger

percentage of nothing" (Rooks, Tr. 1409). Many small bottlers, such as Westminster, Maryland, are surrounded by large bottlers and therefore have no one with which to form a cooperative (Roadcap, Tr. 2467). Small bottlers in a region do not together have the financial resources to withstand the underpricing of large bottlers. For example, the combined sales of the small bottlers in the Philadelphia area "don't come close" to the sales of the Philadelphia Coca-Cola Bottling Company (Levin, Tr. 1938–39). As the Coatesville, Pennsylvania bottler of Coca-Cola also testified, "* * * we could not together merge a large enough factor to even be competitive" with Philadelphia and Baltimore (Filoromo, Tr. 2214).

191. Because it would cost $5 million to $10 million to build the facilities necessary to compete for chain warehouse business, small bottlers acting jointly would still not have the necessary resources to compete with large bottlers (Rooks, Tr. 1419). Joint buying of items such as glass bottles would produce no savings because the glass producers do not provide volume discounts (Filoromo, Tr. 2141). Because of costs arising from shipping distances, a cooperative would not achieve the savings on non-returnables necessary to compete with large bottlers (Ellis, Tr. 1045–46), since the chain store warehouses are in closer proximity to the larger bottlers' plants (Rooks, Tr. 1415–16). [75]

192. Small bottlers would not survive by being acquired by large bottlers (Smith, Tr. 787; Rooks, Tr. 1409–11, Brown, Tr. 1703; Alford, Tr. 2559; Crabtree, Tr. 2688–89). There is no incentive for a large bottler to purchase a small bottler since the large bottler instead could "sit around and simply take his [the small bottler's] business" (Rooks, Tr. 1409). The large bottler would not be interested in using the small bottler as a distributor (Rooks, Tr. 1410–11, 1420–21; Brown, Tr. 1703) because many large bottlers already have distribution centers close to the small bottlers' territories (Crabtree, Tr. 2688); such use would entail purchasing a very expensive manufacturing facility in order to convert it to the distribution warehouse (Crabtree, Tr. 2688); and there would be a decreased need for local distribution in light of the demise of the returnable bottle (Crabtree, Tr. 2688–89). Acquiring the small bottler for use as a marketing bottler is "a theoretical option of no economic value" (Smith, Tr. 788).

193. Many large bottlers would be forced out of business since they do not have the resources to compete against bottling plants owned by the largest bottlers and by subsidiaries of the syrup companies (Ellis, Tr. 1039–40; Stokes, Tr. 1162; Sales, Tr. 1279–80; Navarre, Tr. 1543–46, 1570; Cameron, Tr. 2061–62; Roadcap, Tr. 2460; Clements, Tr. 4051). The Coca-Cola Company and other large national soft drink companies

would survive because of their resources and diversification (Sales, Tr. 1280, 1282; Navarre, Tr. 1546; Levin, Tr. 1936–37). The natural consequence of the demise of more and more bottlers is that ultimately the bottling business would become concentrated in the hands of a very few bottlers for each brand (Smith, Tr. 733, 738). The very few bottling companies would be owned by large companies, publicly held corporatons, and food chains (Clements, Tr. 4051; Sales, Tr. 1281–82). [76]

194. The economic impact on local communities would be substantial with the elimination of exclusive sales territories. Many people employed by bottlers of Coca-Cola and other national brands which would be forced to curtail services or close their doors would be out of jobs, as has happened in the case of small local bakeries and dairies (Sales, Tr. 1266–67, 1294; Levin, Tr. 1924–25). A large number of the approximately 52,000 employees of bottlers of Coca-Cola (RX 35C), many of them long-term employees (Carver, Tr. 1620; Filoromo, Tr. 2212–13), would be discharged as route delivery is curtailed or eliminated (Smith, Tr. 733; Sales, Tr. 1317; Clements, Tr. 4044).

195. Contributions to the economic health of many communities by soft drink bottling companies through payment of taxes, purchase of supplies, and borrowing of money would also decline (Cameron, Tr. 2062; Crabtree, Tr. 2686; Cobetto, Tr. 2840–41; Ippolito, Tr. 3271–72). Many small towns, of which Coatesville, Pennsylvania (Filoromo, Tr. 2212–13), Ada, Oklahoma (Crabtree, Tr. 2686), Herminie, Pennsylvania (Cobetto, Tr. 2840–41), Washington, Pennsylvania (Cameron, Tr. 2062), and Montross, Virginia (Carver, Tr. 1620), are typical, would find one of their larger employers out of business.

DISCUSSION

The Legal Theory on Which the Decision Is Not Based

Complaint counsel specifically disavowed reliance upon a *per se* theory in offering evidence at the hearing of this case (see *Northern Pacific Railway Co.* v. *United States,* 356 U.S. 1 (1958)), preferring rather that the acts alleged to violate Section 5 of the Federal Trade Commission Act be judged according to the rule of reason (Complaint Counsel's Proposed Findings pp. 7–8). Complaint counsel's disavowal is not binding on me; however, in my view, complaint counsel took the proper course, and it is appropriate to explain why the *per se* approach is inappropriate and the rule of reason should be applied. [77]

If the bottlers had agreed as to their exclusive territories, this case would involve horizontal territorial market allocations, *i.e.*, those agreed upon by competitors at the same level of the market structure, and such action would be illegal *per se*. *United States* v. *Topco*

Associates, Inc., 405 U.S. 596, 608 (1972). *But* there is no evidence in this record of an agreement or understanding among the bottlers to divide markets. The evidence shows instead that the exclusive territorial provisions of their contracts were vertically and unilaterally imposed, that is, "Coca-Cola" acted alone in imposing the restrictions and it alone determined the territories. Further, there is no evidence that the territories were agreed upon by bottlers who then had "Coca-Cola" "impose" them. See *United States* v. *Sealy Inc.*, 388 U.S. 350, 352–354 (1967).

The fact that "Coca-Cola" has acquired some bottlers does not transform the system into a horizontal agreement in illegal restraint of trade. See *White Motor Co.* v. *United States*, 372 U.S. 253 at 258 (1963) where White in its agreements with its dealers retained the exclusive right to sell ". . . trucks to Federal and State governments or any department or political subdivision thereof . . ." and the Supreme Court declined to base its decision on a *per se* theory.

Vertical territorial allocations such as those disclosed on this record are not illegal *per se*. After declining to intimate its view as to the legality of a vertical arrangement by a manufacturer restricting the territory of his distributors and dealers, the Supreme Court in *White Motor, supra*, 372 U.S. at 263, distinguished between horizontal and vertical restraints: [78]

> Horizontal territiorial limitations, like group boycotts or concerted refusals by traders to deal with other traders are naked restraints of trade with no purpose except stifling of competition. A vertical territorial limitation may or may not have that purpose or effect. . . . They may be too dangerous to sanction or they may be allowable protections against aggressive competitors or the only practicable means a small company has for breaking into or staying in business and within the rule of reason.

It also is well established that a territorial representation agreement between a supplier and his customer, which gives the latter exclusive rights in a given area, does not inevitably violate the Sherman Act. See *Schwing Motor Co.* v. *Hudson Sales Corp.*, 138 F. Supp. 899, 902 (D. Md. 1956), *aff'd*, 239 F.2d 176 (4th Cir. 1956), *cert. denied*, 355 U.S. 823 (1957); *Packard Motor Car Co.* v. *Webster Motor Car Co.*, 243 F.2d 418, 420 (D.C. Cir. 1957), *cert. denied*, 355 U.S. 822 (1957); *The Coca-Cola Bottling Co.* v. *The Coca-Cola Co.*, 269 Fed. 796 (D. Del 1920). The Supreme Court held in *United States* v. *Arnold, Schwinn & Co.*, 388 U.S. 365, at 376 (1967), referring to *United States* v. *Colgate & Co.*, 250 U.S. 300 (1919), that if equivalent, competitive products are readily available in the market, an exclusive representation agreement between supplier and customer is not in and of itself unlawful. The record in this proceeding amply demonstrates that there are numerous equivalent brands of soft drinks available both nationally and more importantly in the markets comprising bottler's territories (Findings 92–102).

The Court did state in *Schwinn* that the Sherman Act was violated when the manufacturer imposed upon the dealers to whom the manufacturer *sold* goods, restrictions as to the customers to whom the dealers could resell: "[I]t is unreasonable, without more, for a manufacturer to seek to restrict and confine areas or persons with which an article may be traded after the manufacturer has parted with dominion over it." 388 U.S. at 379. But the Court added that ". . . [79] the vertically imposed distribution restraints *absent* price fixing and in the presence of adequate sources of alternative products to meet the needs of the unfranchised—may not be held to be *per se* violations of the Sherman Act." 388 U.S. at 381.

I do not believe the "unreasonable without more" language in *Schwinn* does or that it was intended to apply to restrictions imposed incidental to the grant of a trademark license such as the one "Coca-Cola" and the other national bottlers use. In fact, in *Schwinn, supra*, 388 U.S. at 379 n.6, the Supreme Court expressly declined to consider whether a patentee has any greater rights to reserve control over the destiny of the product manufactured or the conditions of its resale. And more recently a U.S. District Court Judge held in *Jack Winter, Inc.* v. *Koratron Co., Inc.*, 375 F. Supp. 1, 63 n.87 (N.D. Cal. 1974), that the question of a trademark licensor's rights fall within this reservation. *Cf.* p. 31, Report of Ad Hoc Committee on Franchising, FTC Staff Report at 31 (June 2, 1969) (RX 109Z5).

"Coca-Cola" has not parted with dominion over the product it sells, and it does not sell its bottlers a finished product for resale. Rather, it sells (a) the right to use its trademark and (b) a syrup or concentrate made from a secret formula. The bottler manufactures a finished product according to the licensor's—"Coca-Cola's" —specifications, using its own facilities and supplies. In addition, in the agreements with its bottlers, "Coca-Cola" reserves the right to make quality inspections and these reasons the "unreasonable without more" —*per se*—language in *Schwinn* is not controlling in this case. [80]

There is no doubt that if a dealer in or a distributor of a product is insulated from sales by contiguous or other dealers observing the territorial restraints a manufacturer has imposed, the restraint raises questions which have arisen for many years under the antitrust laws and Section 5 of the Federal Trade Commission Act. See *Dr. Miles Medical Co.* v. *John D. Park & Sons Co.*, 220 U.S. 373, 404–408 (1911); *Snap-On Tools Corp.* v. *FTC*, 321 F.2d 825 (7th Cir. 1963); *Sandura Co.* v. *FTC*, 339 F.2d 847 (6th Cir. 1964). A restraint is illegal *per se* if it has such a pernicious effect on competition and is so lacking of any redeeming virtue that it is conclusively presumed to be unreasonable without elaborate inquiry as to the precise harm caused. (See *Northern Pacific Ry. Co., supra,* 356 U.S. at 5.) Agreements to fix prices, group boycotts, tying arrangements and horizontal divisions of markets by competitors, for several examples, none of which are present here, have been held to be *per se* violations. A unilaterally imposed territorial sales restriction which forms a part of the scheme or agreement *to fix prices* is violative *per se* of the antitrust laws. *Schwinn, supra,* 388 U.S. at 373. The facts brought to light here do not reveal an effect on competition so pernicious as to warrant *per se* treatment.

The Commission's view is succinctly stated in *Holiday Magic, Inc.*, Dkt. 8834, [84 F.T.C. 748 at 1057] 3 TRR ¶20,757 at 20,623 (1974): "Here, as in *Adolf Coors Co.*, [Dkt. 8845, [83 F.T.C. 32] 3 TRR ¶20,403 (1973)] imposition of exclusive territories was accompanied by price fixing, and that combination renders the use of exclusive territories illegal *per se.*" *But* there is no evidence in this case that there was any scheme or agreement on the part of "Coca-Cola" or effect from its actions which fixed prices (Findings 34 and 66). What is more, "Coca-Cola" did not and does not (1) tie its licenses to the purchase of other products the company might supply (Finding 66), (2) preclude bottlers from manufacturing other brands of soft drinks (Finding 70), or (3) otherwise limit the business activities of its bottler licensees. [81]

Respondents' bottlers not only were and are free to sell in accordance with their own judgment as to what the price was and is to be, but also are free to conduct their business as they see fit. It is worthy of mention that no bottler witness who testified said that the territorial limitations infringed on his freedom to operate his business as *he* thinks is best.

Since the evidence in this matter contains no persuasive evidence suggesting that a *per se* approach should be used, it has been decided under the rule of reason. That is the basis on which the litigative hearings were held and that is the basis on which this initial decision has been prepared.

The Rule of Reason

The rule of reason is the alternative to the *per se* theory for deciding whether a trade restraint is legal. The rule of reason concept stems from *Standard Oil Co.* v. *United States,* 221 U.S. 1, 62 (1911). *Chicago Board of Trade* v. *United States,* 246 U.S. 231 (1918), which was brought under the Sherman Act, is, and again was very recently recognized to be, the landmark case defining the parameters of the rule of reason. (See *American Motor Inns, Inc.* v. *Holiday Inns, Inc.*, 365 F. Supp. 1073 (D.N.J. 1973), *aff'd in part, rev'd in part*, 1975-2 Trade Cases, ¶60,390, at 66,721 (3rd Cir. 1975).)

In contrast with its absence here, *Chicago Board of Trade* involved a form of horizontal price fixing by reason of the Board's rule holding a price firm from the close of business one day to the start of business on the next. In the decision, however, Justice Brandeis explained the ground rules for determining whether a restraint on trade is reasonable (246 U.S. at 238): [82]

> Every agreement concerning trade, every regulation of trade, restrains. To bind, to restrain, is of their very essence. The true test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition, or whether it is such as may suppress or even destroy competition. To determine that question the court must ordinarily consider the facts peculiar to the business to which the restraint is applied; its condition before and after the restraint was imposed; the nature of the restraint, and its effect, actual or probable. The history of the restraint, the evil believed to exist, the reason for adopting the particular remedy, the purpose or end sought to be obtained, are all relevant facts.

It should be noted that although *Chicago Board of Trade* involved charges brought under the Sherman Act, it was established long ago that charges under that Act are cognizable under Section 5 of the Federal Trade Commission Act (15 U.S.C. 45), *FTC* v. *Cement Institute*, 333 U.S. 683 (1948). "The Federal Trade Commission Act may be construed in *pari materia* with the Sherman and Clayton Acts. 'This construction allows for using cases decided under any of the antitrust laws in cases brought by the Commission.' *Atlantic Refining Co.* v. *Federal Trade Commission*, 344 F.2d 599, 606 (C.A. 6), *cert. denied*, 382 U.S. 939." *American Cyanamid Co., et al.* v. *Federal Trade Commission*, 363 F.2d 757, 770 (6th Cir. 1966).

Consequently, a violation of Section 5 may be found where the "basic policies" of the Sherman Act or the Clayton Act are violated. Beyond this, if the evidence brought forth at the adjudicative hearing warrants it, even though an actual violation of *those* statutes is not found, Section 5 of the FTC Act still may have been violated. *Golden Grain Macaroni Co.* v. *FTC*, 472 F.2d 882, 886 (9th Cir. 1972), citing *FTC* v. *Brown Shoe Co.*, 384 U.S. 316 (1966). However, the Commission has made it clear that, in its view, ". . . [N]ot every method of competition which involves some restriction on competition is an 'unfair method of competition' under the FTC Act" *Sandura, supra*, 339 F.2d at 849. [83]

In making the determination as to whether a method of competition is unfair, ". . . the Federal Trade Commission does not arrogate excessive power to itself if, in measuring a practice against the elusive, but congressionally mandated standard of fairness, it, like a court of equity, considers public values beyond simply those enshrined in the letter or encompassed in the spirit of the antitrust laws." *FTC* v. *Sperry & Hutchinson Co.* (*S&H*), 405 U.S. 233, 244 (1972). The quoted language in *S&H* cuts both ways. That is, the Commission may find or may not find a violation by considering public values beyond those "enshrined" in the antitrust laws. Thus, the Commission is not limited necessarily to consideration of the criteria which Justice Brandeis listed in deciding a case under the rule of reason and has every right to act as a court of equity. For this purpose, the Commission has described guidelines as to what it considers in determining whether a restraint on trade should be held to be violative of Section 5. These guidelines are:

> (1) whether the practice, without necessarily having been previously considered unlawful, offends public policy as it has been established by statutes, the common law, or otherwise—whether, in other words, it is within at least the penumbra of some common-law, statutory, or other established concept of unfairness; (2) whether it is immoral, unethical, oppressive, or unscrupulous; (3) whether it causes substantial injury to consumers (or competitors or other businessmen). *FTC* v. *Sperry & Hutchinson Co.* (*S&H*), 405 U.S. 233, 244–45 n.5 (1972), quoted from Statement of Basis and Purpose of Trade Regulation Rule 408 [Unfair or Deceptive Advertising and Labeling of Cigarettes in Relation to the Health Hazards of Smoking], 29 F.R. 8324, 8355.

[84] Clearly, territorial exclusivity is within the "penumbra" of a concept of unfairness because it does impose a restraint on trade in that a businessman's geographical area of competition is limited. Equally clear is the fact that under the Commission's guidelines territorial exclusivity is legal if it is not immoral, unethical, oppressive or unscrupulous and does not cause substantial injury to consumers, competitors or other businessmen. In my view, the territorial exclusivity Coca-Cola bottlers enjoy is none of these and does not cause substantial injury to anyone.

In keeping with the concept of its sitting as a court of equity, the Commission declined in *S&H* (*supra*) to appraise the allegedly trade-restraining conduct in that case on the basis of *Schwinn*. In its *S&H* opinion, and in harmony with the view that there is a difference between the sale or transfer of a bicycle to a dealer merely for resale and the sale of syrup or concentrate to a bottler for manufacturing another product, the Commission said:

> [W]e do not believe it appropriate to decide the broad competitive questions presented in the record on the narrow and technical basis of a restraint on alienation. The circumstances here are much different from that where products are transferred to a dealer for resale. They are complicated by the nature of the trading stamp scheme. It is essential in this matter, we believe, . . . to determine whether or not there has been or may be an impairment of competition. Thus we intend to look at the substance of the

allegedly illegal practice rather than to decide the case by application of a technical formula. *S&H,* 405 U.S. at 247–248 n.6.

[85] As in *S&H,* the circumstances in this case also are complicated by many factors, including the investments bottlers make, the fact that most of them are relatively small, local businessmen, the nature of "Coca-Cola's" trademark licensing, and its quality-control practices involving inspections, product testing and related activities.

Is the Territorial Restraint Reasonable?

The fact that the territorial restraint is not horizontally agreed upon or coupled with price fixing does not obviate the possibility that the restraint is illegal. This, because it might unreasonably restrain trade in some other way.

The territorial restriction here allows bottlers to enjoy area exclusivity while prohibiting them from shipping Coca-Cola outside their territories and from selling to resellers who may do so. As such, it does eliminate intrabrand competition between Coca-Cola bottlers but the restriction is not necessarily unreasonable for *that* reason. *Snap-On Tools, supra,* 321 F.2d at 831–832; *Sandura, supra,* 339 F.2d at 858–859; *American Motor Inns, supra,* 1975–2 Trade Cases ¶60,390 at 66,720–66,722. Application of the rule of reason was not confined to intrabrand competition in *Schwinn, supra,* 365 U.S. at 382. Consequently, consideration must be given to still other factors.

The initial question to answer is whether the restraint is legal in its purpose. *Chicago Board of Trade, supra,* 246 U.S. at 238. Then, if (1) the purpose is to further legitimate business goals rather than to hinder competition, (2) the restraint is no broader than is reasonably necessary, and (3) it promotes competition by merely regulating it, the restraint is legal. See *U.S.* v. *Addyston Pipe & Steel Co.,* 85 Fed. 271 (6th Cir. 1898), *aff'd,* 175 U.S. 211 (1899); *U.S.* v. *Columbia Pictures Corp.,* 189 F. Supp. 153 at 178 (S.D.N.Y. 1960); *American Motor Inns, supra,* 1975–2 Trade Cases ¶60,390 at 66,722–66,723. [86]

The evidence shows that the territorial exclusivity provision was adopted by "Coca-Cola" for the legitimate purpose of broadening the distribution of Coca-Cola by persuading local businessmen to invest the capital, time and ability required to manufacture and sell Coca-Cola in bottles (Findings 28–31). The vehicle-round-trip-in-one-day measurement "Coca-Cola" used for setting the territorial boundaries (Smith, Tr. 681) was both reasonable and practical and no broader than necessary to provide the bottler licensee with a territory he could serve and develop. Likewise, the evidence shows that exclusive bottler territories continue to serve "Coca-Cola's" legitimate business needs by encouraging a high level of continuing capital investment by bottlers and maintenance of the intensive merchandising and servicing efforts which preserves the widespread availability and high sales of Coca-Cola products (Findings 137-140). Territorial exclusivity also encourages use of returnable bottles (Findings 120-121) which are preferable from the standpoint of economy and environmental impact (Findings 110-126, 167-168).

The territorial provision reasonably regulates competition because it enables the bottler licensee to focus on his own territory and the strong interbrand competition he faces within that marketing area. With a protected territory the bottler need not be concerned over his fellow Coca-Cola bottler licensees being the beneficiary of his efforts to promote and sell Coca-Cola in his territory and his investments in returnable bottles.

The arrangement thus concentrates the bottlers' competitive efforts in the direction of other brands rather than on other bottlers of Coca-Cola (*i.e.*, interbrand instead of intrabrand competition). This difference in the interests of bottlers of different brands should generate a stronger competitive effort than would be the case if those efforts were diluted by also being directed toward other Coca-Cola bottlers. The result is that territorial exclusivity leads to greater rather than lessened competition in the soft drink industry. [87]

Another element to consider in determining whether a restraint is reasonable is the power of the imposer of the restraint in the relevant market. *Columbia Pictures Corp., supra,* 189 F. Supp. at 178. The price setter's market power is determined by his freedom from concern over prices charged by his competitors in the market in which he sells the product. *U.S.* v. *E. I. duPont de Nemours & Co.,* 118 F. Supp. 41 (D. Del. 1953) *aff'd,* 351 U.S. 377, 391-392 (1956). But there is more than adequate evidence in this record to show that in the national soft drink market "Coca-Cola" and other respondents, as well as other national brand licensors, *and* the bottlers in their regional and local markets are *very much* concerned with interbrand prices (Findings 103-109, 127-128). The evidence also shows that market shares of "Coca-Cola" nationally are declining but that locally or regionally in various bottlers' territories the market shares fluctuate in direct response to interbrand competition (Findings 163-166). It also is worthy of mention that bottlers of Coca-Cola face strong intrabrand competition from post-mix Coca-Cola (Finding 133).

Is There an Adverse Effect on Consumers, Competitors or Other Businessmen?

Chicago Board of Trade, supra, also indicates that whether competition is or may be promoted or curtailed by the restraint is a factor to be considered in determining its legality (246 U.S. at 238). As indicated above, the evidence here shows that focusing the bottlers' attention on their own territorial markets stimulates their competitive effort. There is keen interbrand pricing and also packaging competition (Findings 103–109, 149–153) and there are many brands of soft drinks available (Findings 92–102). In the last few years in particular, many new brands of soft drinks have successfully been introduced into the territorial markets of bottlers (Findings 154–162). [88]

The bottlers also compete intensely in having their brands available at a multitude of outlets and in obtaining both desirable shelf-space and display locations in food stores (Findings 137–140, 141–144). *and* it is worth repeating that the prices of Coca-Cola and allied products are determined by the bottlers individually and that those prices are sensitive to the prices of other brands and types of soft drinks (Findings 66, 103–109, 127–131).

What if Exclusive Territories Were Held To Be Illegal?

Declaring "Coca-Cola" territorial exclusivity provisions to be illegal would adversely affect competition because it would lead to the business failure of many small and some large bottlers as well as to the accelerated growth of large bottlers (Findings 183–186, 193). This result would be in direct conflict with the purpose of the Congress in enacting and in agencies administering the antitrust laws ". . . to perpetuate and preserve, for its own sake and in spite of possible cost, an organization of industry in small units which can effectively compete with each other." *U.S.* v. *Aluminum Co. of America,* 148 F.2d 416, 429 (2d Cir. 1945). See also *Brown Shoe Co.* v. *U.S.,* 370 U.S. 294, 333, 344 (1962); *cf. Fashion Originators' Guild* v. *FTC,* 312 U.S. 457, 467 (1941); *cf. Federal Trade Commission* v. *Fred Meyer Inc., et al.,* 390 U.S. 341, 349–351 (1968).

With the failure of small bottlers would go the jobs of the owners and of the thousands of their employees. The contributions to the economies of the areas in which small bottlers and their employees now earn their living would certainly diminish substantially and would disappear completely where the bottler was forced out of business (Findings 194–195).

I do not believe that enforcement of the antitrust laws and of the Federal Trade Commission Act was or is intended by the Congress or the Commission to bring about such a result. For the reasons referred to above, such a holding would be harmful to competition and on the basis of extensive evidence in this record would not lead to any countervailing advantage to the interest of the public in price, quality or availability. [89]

In fact, the probable result would be an increase in prices of soft drinks to consumers because of the elimination of small bottlers and the resulting enhanced market power of those bottlers who would survive along with the eventual reduction in the number of brands which would be marketed (Findings 170, 176, 179). As to these, there is much testimony in the record to the effect that there would be even greater use of cans and non-returnable bottles (Findings 120–121). These are more expensive than returnable bottles and greater use of them probably would lead to higher prices (Finding 110). In addition, industry witnesses testified that the reduction in the number of small bottlers and the resulting growth of large bottlers would lead to a reduction in the number of different brands of soft drinks available (Findings 179–182).

The evidence is convincing that elimination of territorial exclusivity would increase the use of non-returnable bottles and cans (Findings 120–122). This would be contrary to the policy of the Congress in enacting the National Environmental Policy Act (42 U.S.C. 4331(a) (1972)), as follows:

> . . . it is the continuing policy of the Federal Government, in cooperation with State and local governments, and other concerned public and private organizations, to use all practicable means and measures, . . . in a manner calculated to foster and promote the general welfare, to create and maintain conditions under which man and nature can exist in productive harmony, and fulfill the social, economic and other requirements of present and future generations of Americans.

A decision which would lead to even greater use of environmentally undesirable, disposable bottles and cans would not be in harmony with the quote above. The decision in this matter is one means for contributing to accomplishment of the objectives of the legislation. [90]

CONCLUSIONS

Respondents are engaged in commerce and their acts and practices are both "in commerce" and "affect commerce" within the meaning of the Federal Trade Commission Act; hence the Commission has jurisdiction over respondents and their acts and practices.

The territorial exclusivity provisions in the contracts respondents have with their bottlers do in fact restrict intrabrand competition between bottlers. *However*, because of the unique nature of the soft drink industry, the restrictions are not adverse to the interest of the public and they do further the legitimate business goals of respondents; hence, they are not unreasonable restraints on trade. This, because there is substantial and effective interbrand competition in each Coca-Cola bottler's territory in (1) pricing, (2) maintaining product quality, (3) packaging, (4) providing service to retailers and to members of the public, and (5) merchandising.

The territorial exclusivity provisions in the contracts respondents have with their bottlers are no more restrictive than is necessary to persuade bottlers to make and to continue to make the sizable capital investments necessary to operate successfully, to hire and to continue to hire employees to operate the equipment and to contribute to the economies of the communities in which they are located.

Elimination of the territorial exclusivity provisions would have an adverse effect on competition and be contrary to the objectives of the antitrust and environmental impact laws because (1) many small bottlers would be forced out of business with the adverse effects mentioned above, and (2) there would be greater use of non-returnable bottles and cans. Greater use of non-returnable bottles and cans would result in higher prices per ounce of soft drink and greater detriment to the environment. [91]

The adverse effect on intrabrand competition of the territorial exclusivity provisions in respondents' contracts with their bottlers is outweighed by the beneficial effects which those provisions have on interbrand competition in national and local soft drink markets.

ORDER

It is ordered, That the complaint in this matter be, and it is hereby, dismissed.

DISSENTING STATEMENT OF COMMISSIONER CLANTON

In light of the Supreme Court's recent decision in *Continental T.V., Inc.*, v. *GTE Sylvania, Inc.*, 433 U.S. 36 (1977), this case presents important questions about the proper application of the rule of reason in judging the legality of vertical distributional restraints. For the reasons set forth below, I dissent from the majority's ruling and recommend that the case be remanded for further analysis of the effect of exclusive territorial restrictions on interbrand competition in the soft drink industry.[1] [2] Absent evidence of horizontal collusion,[2] the reasonableness of Coca-Cola's territorial restrictions, in my view, can be properly assessed only after examining the competitive state of the soft drink market and the extent to which respondents and their bottlers are capable of exercising market power within this interbrand environment. Although the majority opinion thoroughly analyzes the record and from it presents the best case possible under the circumstances for abrogating Coke's territorial restrictions, I believe the record is insufficient to make a confident judgment about the overall competitive effects of the restraints.

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[1] I adhere to the abbreviations used by the Commission, with the addition of "Maj. Op." to refer to the Majority Opinion and "Oral Arg. II" to refer to the second oral argument conducted on July 28, 1976.

[2] As the majority correctly concludes, there is no evidence that the territorial restrictions were imposed by the bottlers; nor is there any evidence that the restraints have furthered collusive schemes among bottlers or syrup manufacturers.

The majority concludes that the territorial restraints imposed on respondents' bottlers are unreasonable and in violation of Section 5 of the Federal Trade Commission Act.[3] In reaching its decision, the Commission relies on several factors: (1) the elimination of intrabrand competition at the wholesale level;[4] (2) the failure of respondents to provide a convincing justification for the territorial restraints; (3) the adverse effects of piggybacking of brands by bottlers upon the level of interbrand competition; and (4) the prospects for lower wholesale prices due to the interaction between intrabrand and interbrand price competition if the restrictions are removed. Although the Commission finds these restraints to be unreasonable for both refillable and nonrefillable containers, it nevertheless acknowledges that only partial relief is warranted. Accordingly, the Commission's order would permit the continuation of exclusive territories for returnable bottles.[5] Further, recognizing that Coke has a legitimate interest in maintaining the quality of their products at the point of sale, the Commission's order allows the respondent syrup manufacturers to require, *inter alia*, that bottlers take steps to assure that stocks are rotated at retail outlets. [3]

I. SYLVANIA

Before examining the facts of this case, it is essential to review the guidance provided by *Sylvania* for assessing the legality of vertical restrictions under Section 5 of the Federal Trade Commission Act. While not providing definitive standards for applying the rule of reason, the Court cited with approval the classic formulation of the rule in *Chicago Board of Trade*[6] and gave some additional clues for sorting out the complexities of vertical restraints given "their potential for a simultaneous reduction of intrabrand competition and stimulation of interbrand competition."[7] In overturning the *per se* rule of *Schwinn*, the *Sylvania* Court quite clearly indicated that the nature of the restriction—be it territorial, customer or location—is relevant but not controlling.[8] Nor does it appear that the Court intended to limit the legality of vertical restrictions to certain classes of firms such as new entrants or failing or faltering firms.[9] More importantly, the Court emphasized that the critical factor is the effect of these restraints on interbrand competition, noting that such competition "is the primary concern of antitrust law."[10] [4]

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[3] It is unclear, however, whether the Commission's order would bar the imposition of exclusive territories by independent bottlers upon sub-bottlers.

[4] The order would appear to prohibit any limitation on the sales territories of respondents' bottlers although the Commission seems to recognize that other territorial restraints, such as location clauses, may be less restrictive of intrabrand competition. (Maj. Op. at 46 n.41)

[5] Although returnables account for approximately 40 percent of flavored carbonated beverages industrywide (RPF 352), they represent 55 percent of Coke's sales (RPF 348).

[6] *Chicago Board of Trade* v. *United States*, 246 U.S. 231, 238 (1918).

Equally instructive is the Court's extensive discussion of the economic benefits of vertical restraints. Observing that such restrictions may enhance marketing efficiencies and, therefore, the ability of the manufacturer to compete with other brands, the Court cited advantages to both new and established firms.[11] Restrictions imposed by new entrants may help to induce distributors to make necessary investments, while established manufacturers may seek to expand output by encouraging dealers to engage in greater promotional activities or to provide more services. Because of the "free-rider" effect, the Court recognized that dealers might be dissuaded from making expenditures for such investments, advertising, or services.[12] Significantly, the Court concluded that "there is substantial scholarly and judicial authority supporting [the] . . . economic utility" of such restrictions and "relatively little authority to the contrary."[13]

Since Section 5 certainly reflects, at least in part, the policies of the Sherman Act, judicial consideration of territorial restrictions under Section 1 of the Sherman Act necessarily serves to advance the inquiry here. Of course, it is well-established that acts or practices which fall short of violating the Sherman Act may nevertheless traverse the more expansive area of illegality defined by Section 5. But, it is well to remember that: Just as the "rule of reason" has been read into the Sherman Act by *Standard Oil Co. of New Jersey* v. *United States*, 221 U.S. 1, 62, 31 S.Ct. 502, 55 L.Ed. 619, 646 (1911), to allow some competitive practices which restrain competition in some degree, not every method of competition is an "unfair method of competition" under the F.T.C. Act. *Sandura Co.* v. *F.T.C.*, 339 F.2d 847, 849 (6th Cir. 1964).

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[7] 433 U.S. at 51–52.

[8] "[W]e agree with the implicit judgment in *Schwinn*, that a *per se* rule based on the nature of the restriction is, in general, undesirable. Although distinctions can be drawn among the frequently used restrictions, we are inclined to view them as differences of degree and form. (Citations omitted.) We are unable to perceive significant social gain from channeling transactions into one form or another." *Id.* at 58 n.29.

[9] *Id.*

[10] *Id.* at 52 n.19.

[11] *Id.* at 54–57.

[12] *Id.* at 55.

[13] *Id.* at 57–58. It seems clear, of course, that the Court in highlighting the benefits of vertical restrictions did not intend to carve out any classes of transactions which should be treated as *per se* legal. Nor do I support such an approach whether it be by judicial or legislative action.

Recognizing, therefore, that we are measuring respondents' method of distribution against the relatively more-encompassing standard of Section 5, I turn to an examination of the competitive effects of the practice. [5]

II. Intrabrand Competition

At the outset, it is important to recognize what is and is not at issue in this case. There is no disagreement that Coke's system of exclusive territories—in contrast to other types of vertical restrictions, such as location clauses—completely inhibits intrabrand competition.[14] There is also apparently no dispute that the territorial restrictions imposed here were justified at their inception. (*See* Maj. Op. at 10 n.12; 23.) And it is not contended that the restrictions have furthered anticompetitive ends by limiting output or facilitating horizontal collusion among syrup manufacturers or bottlers. Rather, the Commission stresses that the restraints are no longer justified primarily because of changed conditions affecting distribution.

Much is made of the fact that improvements in transportation and central warehousing by food chains have rendered territorial boundaries obsolete, thereby creating inefficiencies and higher prices. Clearly, market conditions today are different than those which existed at the turn of the century. **[6]** Yet to the extent that modern delivery and distribution systems foster inefficiencies, Coca-Cola has an incentive to bring about adjustments which would enhance its bottlers' ability to compete with other brands (at least by means short of inducing more intrabrand competition). This incentive is perhaps enhanced by the fact that Coke's economic leverage vis-a-vis its bottlers is limited — *e.g.*, syrup prices to bottlers may rise only as the price of sugar rises. (CX 9A–G, 11A–B, 13A–B) Hence, Coke's syrup revenues vary proportionately with the sales volume generated by its bottlers.

Where inefficiencies exist, which might make some bottlers less competitive, Coke could be expected to take steps to urge bottler consolidations or other adjustments necessary to enable its bottlers to contend with current competitive realities on an interbrand level. In fact, the record shows that such changes have occurred with the support of Coca-Cola, including 107 consolidations and mergers between 1968 and 1971, 14 temporary marketing bottler agreements by which a bottler who discontinues production continues to distribute Coke produced by a neighboring Coke bottler (Tr. 650–51, CX 1245A–

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[14] This assum[illegible] -mix (or fountain) sales, which are not sold via an exclusive territorial system, are excluded from [illegible], an assumption not accepted by respondents.

M, CX 1246A–J), and several agency arrangements (Maj. Op. at 22 n. 22). Conversely, attainment of scale economies, notwithstanding distributional limitations, may be facilitated for other bottlers by "piggy-backing" several brands and engaging in contract bottling or canning. The record, however, does not afford a thorough evaluation of the trade-offs involved in maximizing operating efficiencies, and provides little insight with respect to the optimal size of a bottler's marketing area.

As for central warehousing, respondent concedes that chains prefer warehouse delivery or plant pick-up rather than direct delivery to their stores. (RPF 88) Nevertheless, the record does not establish a clear cost advantage for central warehouse over store-door delivery. (Maj. Op. at 25 n. 25.) It is at least possible, however, that if this cost advantage were significant, there would be even greater pressure for such service,[15] as well as greater market penetration by brands such as Shasta and others which do not utilize a store-door delivery system. [7]

Of course, it should be kept in mind that, by their very nature, vertical restrictions such as those employed here place constraints on natural market forces. Territorial boundaries, even when first imposed, may not perfectly reflect the parameters of economic markets which would exist if competition were totally unrestrained. That is not to say that considerations relating to the nature of the restraint and its effect on intrabrand competition are irrelevant to the inquiry. But, while legitimate restrictions may become unjustified due to subsequent changes in the market, the significance of the lost intrabrand competition can best be evaluated, as *Sylvania* indicates, in the context of the reasons advanced for imposing such restraints and their effect on interbrand competition.[16]

III. INTERBRAND COMPETITION

A. PROCOMPETITIVE EFFECTS

Respondents offer several justifications for imposing exclusive territories including: (1) inducement of bottlers to make necessary capital investments, (2) more extensive market penetration and increased availability of Coke, (3) greater advertising and promotional efforts by bottlers, (4) quality control, particularly at the distribution level, and (5) preservation of returnable bottles.[17] With respect to the

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[15] In Los Angeles, the chain stores forced bottlers to provide them with warehouse delivery of nonreturnable packages. Alpha Beta, for example, refused store-door delivery of Coke at wholesale prices below the price paid by Alpha Beta to pick up canned Coke at Coke's Los Angeles bottler. (Tr. 3486, 2585–86, 2633–34)

[16] *See* 433 U.S. at 54–55.

[17] Exempting returnables from its order, apparently as an act of discretion in crafting an appropriate remedy, the Commission does not address the possibility that territorial restrictions in the case of returnable containers may be

(Continued)

first four justifications, the majority claims that the strength of the Coke brand provides sufficient incentives for investment, and that any decrease in the current level of bottler advertising will be offset by increases in manufacturer and retailer advertising. Acknowledging that territorial restrictions have increased the availability and market penetration of Coke, the Commission expresses the view that market forces should determine the proper combination of price and availability. In addition, the Commission concludes that the quality of Coke can be maintained at the distribution level through spot checks facilitated by placing bottler identification marks on containers. And, as noted earlier, Coca-Cola may require bottlers to follow specific monitoring and inventory rotation policies. [8]

With respect to capital formation, the majority concedes that exclusive territories provide bottlers with some additional measure of certainty regarding their ability to recover their investments. However, the Commission is unable to conclude that a free market would otherwise render the bottlers incapable of operating at a profit. Granted, Coke's bottlers today need less incentive to make the requisite investment of capital and labor to maintain their competitive position than would a newcomer attempting to enter the market from scratch.[18] Yet the record indicates that a substantial investment is needed to maintain a successful bottling operation.[19] More relevant to our discussion is (1) whether adequate incentives exist for Coke bottlers to maintain the kind of distribution and quality control system utilized here in the absence of territorial restraints, and (2), assuming restrictions are necessary, whether they can be justified in light of their impact on interbrand competition. Since, in my view, the record supports the need for investment incentives to maintain the present marketing system, a point which the majority implicitly concedes as to returnable containers, careful scrutiny of the interbrand effects is required. To say that the current level of capital investment might be unwise in a different competitive milieu (Maj. Op. at 29) simply begs the question of whether such investments enhance or impair interbrand competition.

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justified under the rule of reason and Section 5. Just as I am unable to concur with the majority's decision to prohibit territorial restrictions for nonreturnables, I am reluctant on this record to sanction exclusive territories for refillable containers.

[18] Respondents do not contend that they will be unable to attract bottlers in the absence of territorial restrictions; they do assert, however, that bottlers will have substantially less incentive to make the kind of investments necessary to maintain the current marketing scheme utilizing store-door delivery.

[19] The bottling of flavored carbonated soft drinks is capital intensive, with an investment of $1.00 required for every $1.52 in sales volume. (Tr. 1532) In addition to land and bottling equipment, bottlers must purchase and maintain route trucks and a returnable bottle float. The Coke bottler in Washington, D.C., for example, operates more than 180 route trucks costing $14,000 apiece, and seven tractor-trailer trucks costing $100,000 apiece. (Tr. 1229, 1911–12, 2047–48, 2050, 2456) The Washington bottler, who currently has $2,250,000 to $2,500,000 invested in returnable glass bottles, decided against introducing a 32 oz. returnable bottle in view of the competitive situation and the $1 million investment in glass bottles that would be needed. (Tr. 1262, 1314–15)

Adopting a similar approach, the majority does not challenge the assertions that Coke's territorial restrictions have benefitted interbrand competition by increasing the availability of Coke and fostering greater market penetration than would otherwise be the case. Instead, the Commission suggests that the degree of availability and market penetration currently enjoyed by Coke does not reflect variations in the cost of serving different customers and claims that increased intrabrand competition would allocate market resources more efficiently. (Maj. Op. at 32) Such an analysis falls short of the kind of inquiry demanded by *Sylvania* concerning the procompetitive aspects of the challenged restrictions and their overall effect on interbrand competition. [9]

Exclusive territories, it is argued, facilitate interbrand competition by enhancing availability and output and inducing greater demand for soft drink products. Testimony of record lends support to the view that widespread availability is a significant merchandising factor in this industry. (IDF 137–140) For example, the president of Dr. Pepper testified:

> I will have to start with the fact that soft drinks are an impulse item, and that soft drinks are consumed many times a day by an individual, and in many places. And because of those customs or habits, total availability is essential to provide the opportunity for those people to enjoy. (Tr. 4029)

Dr. Pepper tried distribution of their product via warehouse delivery in Indianapolis and Los Angeles. After finding that Dr. Pepper was not available in numerous small outlets, the company decided that the only way to achieve widespread availability was to use a route delivery system. (Tr. 3996–4000) Similar marketing decisions were made by Lipton and Nestle. (RPF 95–96)[20]

The central feature of this marketing scheme, maximization of availability, is made possible by level pricing, which means that all retail customers in a territory are charged the same price and that some Coca-Cola is provided at less than its actual cost and some is priced above. The record provides no basis, however, for determining whether these cost differentials reflect legitimate promotional considerations or represent a form of price discrimination practiced by firms having a significant degree of market power. (*See* discussion *infra* at 21–22) Furthermore, cost differentials may not warrant the burden of establishing a host of different price schedules.[21] Nor does the record tell us whether consumers would suffer more from reduced competition over availability than they would benefit from the presence of variable pricing and the imposition of minimum delivery and pick-up volume. [10]

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[20] That is not to deny, of course, that more recent entrants to the soft drink business, such as Shasta, have achieved a degree of success without the use of exclusive territories. Such entry, though, has been limited primarily to warehouse delivery of nonreturnables and may, in fact, have been facilitated by increases in demand for soft drink products generated by the very marketing schemes at issue in this case.

[21] For example, under the current store-door delivery system, the expense associated with allocating distribution costs among the numerous outlets served by a bottler may not justify an expanded price list.

On the issue of advertising, the record provides no prognosis of the expected level of interbrand competition if bottlers are given less incentive to advertise Coke to ultimate consumers by virtue of the "free-rider" effect. Coke and its bottlers spent more than $50 million on national cooperative media advertising in 1974 and about half of these expenditures were made by bottlers. (Tr. 652, 685–86) The majority questions the utility to consumers of much of this advertising, some of which is admittedly of the brand enhancement or image type, and suggests that much Coca-Cola advertising is unnecessary in view of Coke's "widely recognized name."

These judgments concerning the quality of Coke's promotional efforts were not based upon a systematic and thorough review of Coke advertising, since such a task would have complicated this proceeding enormously. Yet, even if the Commission could say with any confidence that Coke's advertising conveyed little information of use to consumers, prohibiting exclusive territories might only result in "a shift to less efficient methods of obtaining the same promotional effects." *Sylvania*, 433 U.S. at 56 n. 25. While the Commission concedes that it will be in Coke's interest to assume more of the brand-enhancement burden in the future, the record evidence gives no clue as to the relative efficiency of manufacturer advertising versus bottler advertising.

But the very difficulty of making such fine-tuned assessments only underscores the importance of focusing on broader competitive considerations in weighing the reasonableness of advertising-related or any other justifications.[22] For example, promotion of the Coke brand may have resulted in such a high degree of product differentiation and conferred upon respondents and their bottlers such a substantial amount of market power that the Commission would be justified in striking down the restrictions irrespective of any countervailing benefits. As noted *infra*, however, the record in its present state does not warrant such a conclusion. [11]

With respect to the quality justifications proffered by Coke, there appears to be no dispute that territorial restrictions encourage individual bottlers to produce a high quality product and, through proper rotation of stock, ensure that rigorous quality standards are met until final delivery to the customer. Monitoring the quality of

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[22] The majority conclusion (Maj. Op. at 35) that advertising-related considerations may justify an intrabrand restraint only in the case of new or faltering firms suggests that the Commission has adopted Justice White's concurrence in *Sylvania*, 433 U.S. at 63–65. It is clear, however, that a majority of the Court would not so limit application of a rule of reason analysis. 433 U.S. at 47 n.12, 53–54 n.22, 59.

Coke at the retail level is facilitated because a Coke bottler knows he will be held accountable, on both a public relations and product liability basis, for all Coca-Cola sold within his district. However, applying the underlying rationale of the Commission decision in *Adolph Coors Co.*, 83 F.T.C. 174 (1973), the Commission finds Coke's territorial restrictions to be unreasonable due to the availability of "less anticompetitive means" to the same end, namely, the establishment of reasonable quality control standards, including inventory rotation policies, and a requirement that bottlers place their own identifying mark on each bottle or can. The Commission concludes, however, that territorial restrictions are not "reasonably necessary to ensure the taste uniformity or the purity of these products." (Maj. Op. at 38)

Undoubtedly alternate means are available for ensuring some degree of quality control, though at what cost and with what measure of effectiveness are not ascertainable from the record. That other, if less satisfactory, strategies exist does not by itself render the use of exclusive territories to maintain product quality unreasonable. Such a determination requires further consideration of interbrand competitive effects.

To conclude, as the majority seems to imply, that the availability of suitable marketing approaches less restrictive of intrabrand competition is sufficient to find a violation, places the Commission in the difficult position of having to make its own judgment about the commercial merits of various strategies without regard to their impact on interbrand competition. While such a test may have some support in the case law,[23] it has never been sanctioned by the Supreme Court. Moreover, in rejecting adoption of a "no less restrictive alternative" rule in a recent decision, the Third Circuit highlighted the problems inherent in such a standard: [12]

> Entrepreneurs . . . would then be made guarantors that the imaginations of lawyers could not conjure up some method of achieving the business purpose in question which would result in a somewhat lesser restriction of trade. And courts would be second-guessing business judgments as to what arrangements would or would not provide "adequate" protection for legitimate commercial interests. *American Motor Inns, Inc.* v. *Holiday Inns, Inc.*, 521 F.2d 1230, 1249–1250 (3d Cir. 1975).[24]

Likewise, the Commission's opinion implicitly second-guesses Coke's belief that obstructions to intrabrand competition are needed to maintain the high quality of its product. Yet the record affords no real basis for analyzing the costs or benefits associated with "less restrictive" approaches to support the majority's assessment. While the examination of the business reasons advanced in support of a restraint is certainly an appropriate, indeed necessary, part of the inquiry, that assessment cannot be divorced from interbrand considerations, particularly where, as here, the evidence supports the redemptive value of quality-based and other justifications.

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[23] *White Motor Co.* v. *United States*, 372 U.S. 253, 271 (1963) (Brennan, J., concurring); *Copper Liquor, Inc.* v. *Adolph Coors Co.*, 506 F.2d 934, 947 (5th Cir. 1975); *Siegel* v. *Chicken Delight, Inc.*, 448 F.2d 43, 51 (9th Cir. 1971), *cert. denied* 405 U.S. 955 (1972); *Sandura Co.* v. *F.T.C.*, 339 F.2d 847, 856 (6th Cir. 1964).

[24] The court distinguished *Siegel* and *Cooper Liquor* as involving restraints which were *per se* illegal. *Id.* at 1249. Similarly, the Commission's opinion in *Coors*, upon which the majority relies, found Coors' territorial and warehouse delivery restrictions illegal *per se*. *Coors*, 83 F.T.C. at 194–95 (1973).

On balance, I am unable to conclude from the record before us that the restrictions imposed here are not reasonably related to the marketing strategy employed by Coke: enlargement of market coverage through level pricing, store-door delivery to numerous retail outlets, and frequent service to maintain quality. And, I cannot conclude on the basis of this record that such strategy has so little redeeming competitive virtue that we may dispense with further consideration of interbrand effects. Like any marketing approach, Coke's strategy involves a trade-off between different combinations of price and nonprice competition, but one's preference for one kind of competition over another should not automatically condemn that strategy.[25] In short, the reasonableness of the restraints cannot be judged in isolation from their overall impact on competition. That is the critical factor at issue here. **[13]**

Notwithstanding the Court's express recognition in *Sylvania* of justifications similar to those advanced here, the Commission appears to be taking the position that the kind of competition fostered by the vertical restrictions in this case is inherently less desirable than the competition which would otherwise occur in the absence of such restraints, at least where well-established, successful firms are concerned. Indeed, the majority decision comes close to establishing a *per se* standard of illegality where territorial restraints are imposed by leading firms in an industry, a result seemingly inconsistent with *Sylvania*.

B. ANTICOMPETITIVE EFFECTS

This conclusion is reinforced by the Commission's discussion of the adverse effects of the restrictions on interbrand price competition and its finding that these effects are so substantially adverse as to place upon respondents the burden of showing that the net effect of the restraint is procompetitive. These ill-effects, it is alleged, are evidenced by price disparities among brands sold in adjacent territories and testimony that wholesale prices to some customers would be lower if the restrictions were removed. (Maj. Op. at 47–51) That, in my view, is wholly insufficient as a basis for voiding such restraints. The absence of price uniformity among territories, without additional data such as pricing trends (including their magnitude and duration) or differences in profit margins, is not by itself conclusive and may only suggest that competition is not static and that its intensity and form are likely to vary over time.[26] Indeed, price uniformity among brands and throughout various territories might give rise to even greater alarm. As for the prospect of lower wholesale prices, the evidence at most suggests that greater price competition will occur with [14] respect to chain stores sales, which represent approximately 20–30 percent of Coke's volume nationwide (RPF 325).[27] There is no evidence that lower prices and greater availability overall will occur upon removal of Coke's territorial restrictions.

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[25] It may be true that the procompetitive effects of these restrictions might be greater were they imposed by a new entrant or other firm seeking to challenge the industry leaders. Nevertheless, I am not persuaded by either legal or economic reasons that their use should be so limited.

That some measure of additional price competition might result in certain situations is not unique to this type of restraint or this case, as the Supreme Court implicitly recognized in *Sylvania*. The majority's analysis, regrettably, provides no framework for assessing the impact of the territorial restraints upon the overall competitive structure of the soft drink industry. Concluding that competition might function differently were the restrictions lifted doesn't tell us whether interbrand competition is better or worse off because of these restrictions. The more relevant question, which cannot be answered by recourse to this record, is whether the system of exclusive territories has enabled Coke and its bottlers to obtain an unreasonable degree of market power or exploit such power unreasonably.

The Commission correctly asserts that proof of monopoly power or unrestricted market power, as argued by respondents, is an unnecessary prerequisite to a finding that a particular restraint is unreasonable (Maj. Op. at 18). Citing *Sylvania* for the proposition that a less sweeping restraint than Coke's exclusive territories might be unreasonable for a company with a small market share standing in the shadows of [15] a dominant firm,[28] the Commission adopts the view that an inquiry into the market power of Coke is unessential. (Maj. Op. at 19)[29] Nevertheless, without relying on such a showing, the majority opinion displays the limited, though incomplete, evidence of market power contained in the record. (*See* Maj. Op. at 30 n.30, 34–35, 39–40 n.37, 44 n.40)[30] [16]

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[26] The Commission expresses concern for the "competitive dynamics" of the soft drink industry, (Maj. Op. at 19), but its decision is premised upon a static analysis of prices. Thus, the record contains comparative territorial pricing data for Coke, Pepsi, Shasta, and Green Spot for a single day, July 15, 1971. (Because this data reflects list prices and does not account for promotional discounts, the Commission has little information regarding transaction prices.) While complaint counsel introduced no evidence to demonstrate the variability of these prices over time, there is some anecdotal evidence of the responsiveness of Coke to price adjustments of other brands, and vice versa. (IDF 103–109)

[27] The Coke executive quoted by the Commission (Maj. Op. at 50) to support its belief that prices would fall to principal customers explained in the next breath that the invalidation of territorial restrictions "would mean that we might be faced with either selling to a chain store in a warehouse delivered situation at a low price, and at a higher price to our smaller stores that we were still giving store-door delivery to." (Tr. 993; *see also* Tr. 1000–01.) Other industry witnesses also expressed the view that wholesale prices to non-chain stores would increase in the absence of territorial restrictions. (Tr. 659, 993, 1001, 1003–04, 1152, 1401, 1472, 1572, 1929, 1992, 2066, 2187–88, 2462, 2637, 2686, 2898, 2980, 3054–55, 3500–01, 3583–84, 4036.)

These expected price differences not only will reflect lower bottler costs associated with warehouse delivery, but they also allegedly will result from bottler efforts to skim off the high volume chain store accounts. Respondents argue that bottlers who successfully capture those accounts will have less incentive to continue service to smaller, less profitable outlets. Conversely, other bottlers will be forced to raise prices to smaller accounts to compensate for the lost chain business. (Ans.Br. at 54–58) While this scenario may not prove correct, the record provides no firm basis for concluding otherwise.

That the Commission should dispute the relevancy of market power is somewhat peculiar. The analysis and approval of vertical restrictions in the context of consignment transactions in *Schwinn* illustrates the significance attached by the Court to Schwinn's declining market share and the availability of other competitive bicycles despite Schwinn's claim of product excellence.[31] Similarly, in *Sylvania* the Court made clear that the level of interbrand competition confronting the manufacturer was a crucial consideration in analyzing a vertical restraint, taking note of market share data available in that case although it had been tried on a *per se* theory.[32] Obviously, the greater

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[28] Sylvania had 5 percent of national television sales and 15 percent of television sales in the Sacramento area. *Sylvania*, 433 U.S. at 39 n.6.

[29] Complaint counsel share this view, as expressed in their Reply Brief:

> "Contrary to the assertions of respondents . . . 'market power' considerations, either by way of presence or absence, are not controlling as to the issues herein. The Commission's complaint does not rest upon allegations of market power resident in respondents. Its allegations which charge violation of Section 5 of the Federal Trade Commission Act are predicated solely upon the elimination of intrabrand competition. No allegations with respect to 'substantiality' or 'section of the country' appear in the text of the complaint, and there is no basis for inferring that complaint counsel have the obligation of proving either of these elements as a part of their *prima facie* showing. Exclusive territorial licenses are unlawful because they eliminate intrabrand competition." (Rep.Br. at 16)

[30] Although it is perhaps difficult to argue that "the most widely recognized name in American commerce" does not possess some degree of market power, we cannot take judicial notice of Coke's market power. To be sure, there is some market share data contained in the record, although complaint counsel and respondents agreed not to admit it for purposes of establishing any relevant product market. (Stipulation No. 5; RX 2A). Assuming delineation of a proper product market or submarket, these shares are not insignificant. Such data, however, allows calculations only of a two-firm concentration ratio representing the combined share of Coke and Pepsi. While complaint counsel and respondents agreed to a stipulation setting forth the top four brands in 36 metropolitan areas of the country, only numerical rankings, and not market shares, are given. (Stipulation No. 5; RX 2Z2–2Z38) Moreover, as the Commission points out (Maj. Op. 39–41 n.37), the market share figures found in the record and relied upon by the law judge represent sales to food stores rather than the complete universe of Coca-Cola and Pepsi-Cola sales, and are unable to provide an accurate indication of Coke's syrup sales to bottlers or bottlers' sales of finished soft drink.

Further observations should be made, however, with respect to this data. First, Coke's share of 20.8 percent for statistical case sales of flavored carbonated soft drinks to food stores in 1971 conceals a large measure of variability from region to region. For example, although Coke accounted for 33.2 percent and 33.1 percent of sales in the Southeast and the Southwest, respectively, it was responsible for only 13.1 percent of sales in the metropolitan Chicago region, 14.6 percent of sales in New England, and 14.7 percent of sales in the Pacific region. (Stipulation No. 5; RX 2D–2E) Second, Coke's market share is ironically largest for returnables, the sole container permitted by the Commission to be sold via exclusive territories. Thus, measured on a physical case basis, Coke's sales represented 32.1 percent of all returnable bottles sold in 1971, 17.3 percent of all nonreturnables, and 12.6 percent of all cans. (Stipulation No. 2; RX 2H)

[31] *United States* v. *Arnold, Schwinn & Co.*, 388 U.S. 365, 381–82 (1967). Schwinn's market share had fallen from 22.5 percent in 1951 to 12.8 percent in 1961. *Schwinn, Id.* at 368.

[32] *Sylvania*, 433 U.S. at 52 n.19. In a pre-*Sylvania* case, *American Motor Inns, Inc.* v. *Holiday Inns, Inc.*, 521 F.2d 1230 (3d Cir. 1975), the Third Circuit rejected the district court's finding that a restriction on a Holiday Inn franchisee's ownership of non-Holiday Inn motels was unreasonable. Among other things, the court of appeals noted that the lower court's conclusions did not demonstrate "that considerations like the number or size of the firms in the

(Continued)

the market power of respondents, the less they need fear competition from their rivals and the easier it is for that market power to be transferred through the distribution chain. [17]

The majority opinion also downplays the significance of product market delineation and assessment of the overall level of interbrand competition currently prevailing in that market.[33] Rather than employing the kind of product market analysis which it uses elsewhere to minimize competition between bottlers and independent syrup jobbers (Maj. Op. at 19–21), the Commission notes that the complaint and trial focused upon a market which included virtually every liquid a person might consume, other than alcoholic beverages, and that testimony of industry witnesses concentrated on another market, *viz* flavored carbonated soft drink beverages. (Maj. Op. at 19 n.21) Although a broader market may be more favorable to respondents as the majority suggests, the record unfortunately does not provide a satisfactory basis for assessing Coke's position in that or any other market.

The lack of an adequate record basis for establishing an appropriate product market carries over to analysis of the present level of interbrand competition. Admitting only that the market is not "devoid of interbrand competition," (Maj. Op. at 19) the Commission views its task as limited to arguing the following propositions: (1) that interbrand competition is not as vigorous as one might expect due to "piggybacking"; (2) that industrywide resort to territorial restrictions exacerbates the adverse effect on interbrand competition that results from an individual Coke bottler being unable to compete with other brands beyond his territory; and (3) that enhanced competition among Coke bottlers will result in greater interbrand competition due to the sensitivity of other brands to the price of Coke. (Maj. Op. at 51–52) [18]

The majority contends that piggybacking, rather than enhancing competition, reflects even greater concentration at the bottler level. Obviously, piggybacking of different brands by the same bottler leads to less competition for the patronage of retailers than would otherwise occur if each brand were sold by a separate bottler. If the choice is between a market of single brand bottlers and a market with the same

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industry or [Holiday Inn's] market share played any part in the Court's decision on this question." *Id.* at 1247–48 (citations omitted) And, as the Commission itself indicated in *Coors, supra:*

> "It is where the manufacturer of a branded item possesses substantial market power – the power to set prices irrespective of interbrand competition - that vertical territorial restrictions are especially pernicious, for they eliminate the possibility of interbrand competition which in an imperfect market is a critical supplement to competition between and among different brands." (83 F.T.C. at 196)

[33] One commentator has urged that in adjudicating a vertical territorial restriction under the rule of reason, the factfinder should consider such factors as (1) the percentage of business controlled, (2) the strength of the remaining competition, and (3) whether the action stems from business requirements or purpose to monopolize. J. von Kalinowski, *The Per Se Doctrine – An Emerging Philosophy of Antitrust Law*, 11 U.C.L.A. L.Rev. 569, 589 (1964). Cf. *United States* v. *Columbia Steel Co.*, 334 U.S. 495, 527 (1948).

number of bottlers (and equivalent bottler concentration) offering more soft drink products, our choice would obviously be for the latter. Yet, reliance by new entrants on existing channels of distribution may also reflect high entry barriers into bottling owing in part to the major brands' ability to successfully differentiate their products. At the same time, the freedom of bottlers to carry other brands may signal greater competition among syrup manufacturers for the custom of bottlers.[34] Additionally, there is some evidence of record that, by lowering entry barriers, piggybacking has enabled certain brands to enter the market which would otherwise be unable to afford the steep capital requirements of bottling. (IDF 159–162) Thus, piggybacking is a complex factor in this industry and, like vertical restraints, capable of having procompetitive as well as anticompetitive consequences. Given the ambiguity surrounding the proper product market, and the absence of useful market share data, the competitive effects of piggybacking cannot be adequately assessed.

The Commission also expresses concern over the fact that territorial restrictions prevent, for example, a Coke bottler from competing with a Pepsi bottler in the territory of another Coke bottler, and likewise inhibit a Pepsi bottler from competing with Coke in the territory of another Pepsi bottler. (Maj. Op. at 45–49) But the fact that Coke or Pepsi bottlers are not potential interbrand competitors in [19] markets adjacent to their territories is an inevitable consequence of exclusive territorial restraints.[35] By underscoring this effect, the implication is that all exclusive territories, whatever their net effect on competition, are beyond the pale. Further, while the widespread use of territorial restrictions in the industry may facilitate parallel pricing policies by reducing the number of bottlers competing for any particular account, the significance of this phenomenon is difficult to evaluate without first examining the extent to which interbrand competition is foreclosed by respondents and other industry members.

The Commission's final argument is that intrabrand competition among Coke bottlers will serve to lower wholesale prices and, because of the price sensitivity (or cross-elasticity of demand) between Coke and rival products, wholesale prices for other flavored carbonated soft drinks, powdered mixes, and noncarbonated drinks are also likely to decline. (Maj. Op. at 50–52) As previously indicated, the record supports the majority's forecast of lower wholesale prices only with respect to chain warehouse sales; other outlets may well face higher prices for Coke. More importantly, the "ripple-effect" on interbrand price competition which the majority asserts will follow from increased intrabrand competition may signify nothing more than that the level of interbrand competition is already substantial. While the record contains evidence that competing brands are price sensitive to coke, there is also evidence that prices of Coca-Cola products are responsive to the pricing policies of competitors. (IDF 104–109) Although price differentials between major and lesser known soft drink brands may, at times, exist—a characteristic which reflects differences in quality, service and promotional effort—more information concerning the size, frequency and duration of such differentials is needed to properly assess their significance. But whatever competitive repercussions may flow from the Commission's order lifting the territorial restrictions, the net effect of such action is impossible to discern without fully examining the parameters of existing competition. [20]

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[34] In sanctioning the use of Schwinn's distribution scheme in the context of consignment transactions, the Supreme Court placed particular emphasis on the fact that Schwinn's distributors and retailers handled other brands of bicycles as well as Schwinn's. *Schwinn*, 388 U.S. at 381.

[35] For rejection of a similar argument, *see Sandura, supra*, 339 F.2d at 854.

C. NEED FOR FURTHER INQUIRY

Unfortunately, the record does not provide adequate insight into these parameters. We are informed that interbrand competition is less vigorous than it might otherwise be without territorial restrictions, but never told whether interbrand competition is or is not presently sufficient to "provide a significant check on the exploitation of intrabrand market power because of the ability of consumers to substitute a different brand of the same product." *Sylvania*, 433 U.S. at 52 n.19.[36] Similarly, while the Commission rejects the justifications offered by respondents, it does not examine the extent to which the alleged efficiencies generated by Coke's territorial scheme "promote interbrand competition." *Sylvania*, 433 U.S. at 54.

The limited record evidence regarding Coke's market power or the intensity of interbrand competition does not, of course, imply that Coke or the other major brands lack substantial market power. Although a rule of reason standard was applied, this case was never tried on a theory which called upon complaint counsel to produce evidence on the issue of market power. In fact, at one point in their appeal brief complaint counsel argue that no degree of interbrand competition—no matter how intense—could legally justify the total elimination of intrabrand competition. App.Br. at 58. Elsewhere, it appears that complaint counsel viewed their burden as one of establishing a *prima facie* case that intrabrand competition had been eliminated, upon which the burden of proof shifted to respondent to establish that the benefits to interbrand competition outweighed the loss of intrabrand competition. (App.Br. at 9, Oral Arg. II at 21–22) Since vertical restraints invariably reduce intrabrand competition, the latter formulation would normally place the entire burden of persuasion upon respondent.[37] [21]

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[36] *See also, American Motor Inns, supra*, 521 F.2d at 1247, where the court of appeals observed that the district court's analysis did not "take into account whether the competition eliminated by the clause is significant in the context of the total competition extant in the industry. . . ."

Given the somewhat confusing state of the law post-*Schwinn* and pre-*Sylvania*, it is understandable that some uncertainty would creep into a case challenging vertical distributional restraints, irrespective of whether a *per se* or rule of reason standard was being applied. In my view, the rationale underlying *Sylvania*, whether applied in a Sherman Act or Section 5 case, requires the Government to show that nonprice vertical restraints are unreasonable, taking into account both intra- and interbrand effects on competition. Although one commentator has suggested otherwise,[38] I do not agree that such a burden is likely to be insurmountable in the vast majority of cases. The indicia for measuring market power are familiar concepts which do not present unmanageable problems of proof in a rule of reason case.

As I have noted, the majority opinion suggests that the lack of continuing business justification for the restrictions is sufficient to establish liability, but some scrutiny is also given to the interbrand effects of the restraints. Indeed, the Commission concludes that a *prima facie* violation has been made out from evidence showing a substantial lessening of both intrabrand and interbrand price competition. It is further contended that respondents have not overcome this showing by evidence that the territorial restraints have had an overriding procompetitive effect. The rule of reason does not preclude adoption of procedural devices such as a standard of presumptive illegality or even a *per se* rule (as *Sylvania* acknowledges) where the circumstances warrant. However, the record in its present state does not justify application of any such device. For these reasons, I believe that the public interest justifies a remand of this case in order to examine more specifically the effect of these restraints on interbrand competition.

The scattered bits of evidence relating to bottler profitability, concentration levels and pricing patterns contained in this record are incomplete and inconclusive for measuring the competitive health of the soft drink industry.[39] Knowledge of Coke's market share over time [22] as well as the level and trend of concentration in the industry would be particularly helpful in assessing the extent to which Coke, either individually or in combination with other firms, exercises market power in the appropriate product market.[40] So too would information concerning the nature and extent of inroads made by new entrants. Such evidence clearly provides one of the best means for measuring the competitive vigor of the market.

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[37] Although *Sylvania* does not specifically address the question of proof, one commentator has suggested that the division of burden urged by complaint counsel here does not accord with the Court's emphasis on the benefits of vertical restraints. Note, *The Supreme Court, 1976 Term*, 91 Harv.L.Rev. 1, 239 n.64 (1977). In any event, it is doubtful whether adoption of such a rule would be appropriate. *See Sandura, supra; Snap-On Tools Corp.* v. *F.T.C.*, 321 F.2d 825 (7th Cir. 1963).

[38] Note, *The Supreme Court, 1976 Term*, 91 Harv.L.Rev. 1, 239 (1977).

[39] For example, although we are told that bottlers earned profits of 2–7 percent on investment (IDF 85), Coke's profitability at both the syrup level and where it is integrated forward into bottling is not disclosed.

Moreover, since the majority relies heavily on testimonial evidence that removal of the restraints will lower Coke's wholesale prices to supermarket chains, a remand would also present an opportunity to develop more evidence regarding the sensitivity of Coke's market share to the prices of other brands, and vice versa. To the extent that Coke loses sales when a competitor cuts prices, brand loyalty (and the pricing independence that it confers) may not be as great as the familiarity of the Coke brand might suggest.[41] Further, more rigorous analysis of profitability at the manufacturer and bottler levels could provide additional insight into the extent of product differentiation and market power in the flavored carbonated soft drink market.

Coke's use of "level-pricing," which in reality may be a form of price discrimination, may also portend the presence of substantial market power.[42] Further inquiry might show, for example, whether "level pricing" represents the traditional effort of a firm with market power to exploit [23] different demand elasticities among its customers.[43] On the other hand, the existence of joint or common costs for different customers suggests that price may deviate from the marginal cost of serving a particular customer without raising an inference of market power.[44] Also, the frequency and size of price promotions and discounts, which the record reveals to occur with some regularity in this industry, may indicate whether price discrimination is having a harmful or benign effect on competition. In short, the evidence of price discrimination displayed here can not alone suffice as a suitable proxy for measuring market power.

Another avenue worth exploring would be to compare the marketing strategies of independent Coke bottlers with those of Coke's subsidiaries. If the arguments raised by the bottlers are valid, one might expect to find Coke's distributors employing similar policies. Of course, even legitimate reasons for imposing the restraints may be insufficient to save them in the face of substantial adverse effects on interbrand competition.

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[40] If the case were remanded, it might be desirable to amend the complaint to plead other product markets, such as flavored carbonated beverages, which are encompassed within the larger soft drink market.

[41] Note, *Restricted Channels of Distribution Under the Sherman Act*, 75 Harv.L.Rev. 795, 833 (1962).

[42] R. Posner, *Antitrust Law: An Economic Perspective*, at 63 (1976); F. Scherer, *Industrial Market Structure and Economic Performance*, at 253–272 (1970).

[43] Uniform pricing on sales that involve different costs might also facilitate collusion among competing bottlers because of the ease of monitoring compliance and detecting cheating. Again, there is no basis on this record to do more than speculate upon the opportunity for collusion.

[44] *Posner, supra* note 36.

Given the more recent development of the nonreturnable, particular attention should be given to the reaction of the market to such new packaging and the effect of exclusive territories on the growth of these new containers. Quite clearly, there has been more entry in this area by Shasta, Frank's, Faygo, and the private brands than there has been with respect to returnable bottles. Indeed, the record contains uncontradicted evidence that competition compelled Coca-Cola to abandon its exclusive reliance on a single size returnable bottle in the mid-1950s and expand into nonreturnable cans and bottles (Tr. 714, 1344). Since the majority ironically limits relief to this form of packaging, further analysis of this development is warranted in a new hearing.[45] [24]

By emphasizing the importance of market power analysis, I am not suggesting there is some magic formula for determining which restraints are legal and which are illegal. The examples highlighted above are only suggestive of the kinds of evidence that might be useful to such an analysis. They are not meant to be exhaustive, nor would proof as to each be required before the restraints could be declared unlawful. Moreover, I do not contend that liability will attach in vertical restraint cases such as this one only upon some showing that one or more competitors in an industry exercise substantial market power. Indeed, there may be instances where intrabrand restrictions are so patently unrelated to legitimate justifications that more intensive market scrutiny proves unnecessary.

The problem with this case, however, is that it did not proceed on a theory requiring complaint counsel to put on evidence of interbrand effects. Given the state of the record, I cannot conclude whether the territorial restrictions should be approved or condemned without a further look at the state of interbrand competition.[46] I am, of course, reluctant to urge remand of a case which already contains a voluminous record and has been in litigation for several years. Nevertheless, in view of the intervening Supreme Court precedent, I believe the public interest would be served by a remand focusing on interbrand competitive considerations.

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[45] The relative market performance and profitability of fountain sales for which exclusive territories are not granted might also assist the inquiry.

[46] In finding the record inadequate, I have not ignored respondents' considerable efforts to paint a rather glowing picture of the competitive vitality of the soft drink market. Yet, evidence that competition is flourishing, such as the variety of flavors and package sizes available, does not point unambiguously to the conclusion that interbrand competition as a whole is healthy. That the record is unsatisfactory, of course, normally would not entitle complaint counsel to another bite at the apple. But where significant changes in the law have occurred, as they have here, I believe complaint counsel should be given an opportunity to make their case in light of these changes.

OPINION

By DOLE, *Commissioner:*

The basic question on this appeal is whether territorial restrictions which eliminate competition among the independent bottlers of Coca-Cola and allied soft drink products are unfair within the meaning of Section 5 of the Federal Trade Commission Act.

I. INTRODUCTION

Respondent Coca-Cola requires little introduction. It is a diversified corporation with interests ranging from steam boilers to orange juice. In 1968 it had consolidated net sales in excess of $1.1 billion and consolidated assets exceeding $802 million. Pertinent to the issues raised in the complaint in this proceeding are the operations of its Coca-Cola USA division. It is this division which manufactures and sells the soft drink syrups and concentrates used in the [2] processing of finished flavored carbonated soft drinks sold under one or more of the trade names licensed by respondents to the bottlers.[1] In 1968 its syrup sales to bottlers exceeded $246 million.

Around the turn of this century, The Coca-Cola Company sold its right to bottle Coca-Cola and licensed the "Coca-Cola" trademark, in perpetuity, to private investors who, as independent businessmen, operated their own bottling facilities within assigned territories.[2] At the time, The Coca-Cola Company itself produced no bottled soft drinks, and although it does today in certain areas of the country, its entry into the business of bottling the products which bear its trademarks results from the reacquisition of the bottling rights which had been previously granted to local bottlers. Today it operates 27 bottling plants which serve exclusive territories[3] [3] encompassing about 14 percent of the population of the U.S. (RPF 44; Tr. 828, 844).[4]

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[1] In addition to Coca-Cola syrup, The Coca-Cola Company manufactures the key syrup and concentrate ingredients for several other soft drink products. These products, including Sprite, Fresca, Fanta, TAB, and Mr. PiBB, are collectively referred to as "allied products." The first of these, Sprite and Fanta, were introduced in the early 1960s. (Tr. 518–19, 692).

[2] The Thomas Company respondents are the successors in interest of J.B. Thomas, one of the original purchasers of Coca-Cola bottling rights, whose exclusive territory covered states in the South, Southeast, and northward along the eastern seaboard to New York. Respondent Thomas Company granted exclusive bottling licenses to numerous independent bottlers in Alabama, Delaware, Indiana, Maryland, Mississippi, New Jersey, New York, North Carolina, Ohio, Pennsylvania, Virginia, and West Virginia. The Thomas Works respondent licensed bottlers in Alabama, Georgia, Kentucky, and Tennessee. Respondent Works 3rd, Inc., granted exclusive bottling licenses to bottlers located principally in Pennsylvania and New Jersey.

[3] A subsidiary of The Coca-Cola Company, Canners for Coca-Cola Bottlers, Inc., as its name implies, operates canning plants which produce canned soft drinks for the bottlers. In 1974, 42 percent of the canned product of this subsidiary was produced for the bottling subsidiaries of respondent Coca-Cola, 38 percent was produced for the independent bottlers, and 20 percent was produced for sales overseas. (Tr. 846).

[4] The following abbreviations are used for citations:

ID - Initial Decision of the Administrative Law Judge;
IDF - Initial Decision Finding;

(Continued)

The rest of respondents' bottlers are relatively independent businessmen who conduct their commercial affairs as they see fit, subject to three key limitations:

First, when The Coca-Cola Company decided to sell the rights to bottle its product, it agreed to sell to its bottlers a continuous supply of the necessary soft drink syrups, but it refused to yield the secret Coca-Cola syrup formula which would have enabled the bottlers to produce the syrup themselves. Later, when the allied products were introduced, it adopted a similar policy. As a result, respondent The Coca-Cola Company is the bottlers' only source of vital Coca-Cola and allied product syrups or concentrates used in the preparation of the finished soft drinks.[5]

Second, respondent Coca-Cola has retained the right to establish quality standards for the products which carry its trademarks and to insist that the bottlers maintain those standards. Failure on the part of a bottler to meet the quality standards it has established may trigger one of the few contingencies justifying the forfeiture of a bottler's bottling rights. (Tr. 778). [4]

Third, respondents have imposed, by contract, and have enforced, in practice, the territorial restrictions which prevent these independent soft drink bottlers from competing with one another in the sale of bottled, canned, and pre-mixed Coca-Cola and the allied soft drink products made from the syrups and concentrate ingredients produced by The Coca-Cola Company.[6] It is this latter interference with the

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Tr. - Transcript of Testimony;
CX - Commission Exhibit;
RX - Respondents' Exhibit;
App. Br. - Complaint Counsel's Appeal Brief;
Ans. Br. - Respondents' Answering Brief;
Rep. Br. - Complaint Counsel's Reply Briefs;
CPF - Complaint Counsel's Proposed Findings of Fact;
RPF - Respondents' Proposed Findings of Fact;
IPF - Intervenors' Proposed Findings of Fact.

Unless otherwise indicated, "respondent" in the singular refers to The Coca-Cola Company.

[5] The bottler purchases these ingredients from respondent Coca-Cola, and if he was originally licensed to bottle Coca-Cola by one of the Thomas Company respondents, the Thomas Company receives a copy of the purchase order and a commission on the sale. (Tr. 681, 817–18, 855).

[6] Respondents make no attempt to understate their firmness in enforcing these restrictions. (Tr. 669). As a consequence, border disputes involving sales of bottled and canned Coca-Cola and allied products by one bottler into the territory of another are rare and usually insignificant. (RPF 47–54, IDF 68–65). According to the testimony of Mr. J. Lucian Smith, President of The Coca-Cola Company, respondents have a system to detect unusually large syrup orders by a bottler which may indicate extra-territorial sales. Moreover, respondents candidly submit that:

> If an instance of transshipment is brought to the attention of The Coca-Cola Company, it will attempt to contact the bottler from whose territory the product was alleged to have come, and almost always "the bottler does what he can to stop the practice." (RPF 54).

Should a bottler refuse to heed such a warning, his supply of syrup or concentrates may be rationed. Thus:

> . . . in Taft, California, when it was clear that a bottler was purchasing extra quantities of Coca-Cola syrup for the purpose of selling Coca-Cola in cans outside his territory. (sic) The Coca-Cola Company sold the bottler only enough syrup to meet existing demands and likely growth in demand within his territory. (RPF 54).

Respondents have, for the better part of this century, successfully confined their bottlers geographically and prevented intrabrand competition among the bottlers in the sale of Coca-Cola and allied products in bottles and cans.

bottlers' geographic markets which resulted in the complaint now before us. In essence, this complaint alleges that these territorial [5] restrictions injure competition among the bottlers and deprive retailers and consumers of the benefits of open competition in the sale of Coca-Cola and the allied products packaged in bottles and cans.[7]

After a lengthy trial which delved in detail into the day-to-day business of bottling soft drinks the administrative law judge issued his initial decision in which he concluded that territorial restrictions are, in the context of the soft drink industry, procompetitive. Accordingly, he entered an order dismissing the complaint, and counsel supporting the complaint have appealed.

In addition to complaint counsel and the named co-respondents there are 14 independent Coke bottlers and the Coca-Cola Bottlers Association taking part in these proceedings. In 1971 this association included 99 percent of the domestic bottlers of Coca-Cola. At various times during the pretrial, these bottlers and their association were granted leave to intervene with rights of full participation before the administrative law judge. The intervenors filed briefs on appeal and were afforded time to present oral argument before the Commission. Also participating at the oral argument and on brief were Consumers Union, Consumer Federation of America, and National Consumer Congress. The consumer organizations were, by order entered March 2, 1976, granted leave to appear, amici curiae, and the respondents and intervenors were authorized to file additional briefs in response to amici.

We have carefully reviewed the arguments advanced in briefs and at oral argument in light of the record and the initial decision and have concluded, for the reasons stated below, that the territorial restraints respondents impose on their independent bottlers are unreasonable and in violation of Section 5 of the Federal Trade Commission Act. Our order will lift the restrictions which place limitations on the sale of Coca-Cola and allied products packaged in pre-mix containers, or in nonrefillable, nonreusable bottles and cans. For reasons discussed in detail later in this opinion, we find it unnecessary to disturb the exclusive territorial relationships with respect to the sale of these products packaged in returnable, refillable bottles. The Commission has also given careful consideration [6] to the arguments of respondents and the bottler intervenors advocating geographic market segmentation as a legitimate method of protecting "small" bottlers from intrabrand competition. We have reviewed, in-depth, the evidence and the precedents cited in support of this contention, and have concluded that this argument is without merit. Accordingly, we hereby vacate the judge's order dismissing the complaint and his findings of fact and conclusions[8] and substitute in their place the findings and conclusions noted in this opinion.

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[7] Each respondent is engaged in commerce as "commerce" is defined in Section 5 of the Federal Trade Commission Act, and the acts and practices challenged in this proceeding occur in the course of such commerce. (CPF 668–681; CX 59–72; Tr.812–17, 664–65; RPF 50–54).

II. Scope of Review

A. CLASSIFYING THE RESTRAINTS

In their briefs on appeal, both amici and complaint counsel contend that these restrictions are unlawful; complaint counsel believe that the trial record as a whole will, upon *de novo* review by the Commission, demonstrate that the challenged practice constitutes an unreasonable vertical restraint of trade. They also take an alternative position: that the restraints are per se illegal horizontal market division agreements. (App. Br. p. 10). The consumer organizations, appearing amici curiae, urge that the practices be declared per se illegal horizontal and vertical restraints on the distribution of Coca-Cola and the allied products under the Supreme Court's decisions in *Schwinn*[9] and *Topco*.[10] While the appeal in this matter was pending, however, the Supreme Court in [7] *Continental T.V., Inc.* v. *GTE Sylvania, Inc.*, 433 U.S. 36, 1977-1 Trade Cases, ¶61,488 (1977), overruled the vertical per se rule stated in *Schwinn*, but it did not rule out the application of a per se standard in appropriate vertical restraint cases. The court noted that in overruling *Schwinn:*

> . . . we do not foreclose the possibility that particular applications of vertical restrictions might justify per se prohibition under *Northern Pac. R. Co.* But we do make it clear that departure from the rule of reason standard must be based upon demonstrable economic effect rather than - as in *Schwinn* - upon formalistic line drawing (*Id.* at 71,902).

In the aftermath of *GTE*, *Topco*-type market division agreements among competitors clearly remain per se illegal (*GTE*, *supra* at 71,901 fn. 28), while supplier-imposed vertical territorial restrictions must generally be policed under the rule of reason unless it can be demonstrated that, in a particular situation, they typically have or are likely to have a "pernicious effect on competition" and that they "lack . . . any redeeming virtue. . . ." (*Id.* at 71,902). Under the court's most recent pronouncement, then, the first step in evaluating these restraints is to classify them as horizontal or vertical.

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[8] A comparison of respondents' proposed findings and briefs with the initial decision shows that respondents and the judge were of like mind to an extraordinary degree on all key disputed issues. We have carefully considered each of these findings in light of our own de novo review of the entire record and have determined that the judge erred in the legal and factual conclusions which he drew from the evidence. For example, *compare* IDF 183-187 *with* RPF 326-329; IDF 188, 189 *with* RPF 333; IDF 190, 191 *with* RPF 336; IDF 192 *with* RPF 337; IDF 193 *with* RPF 339; IDF 194, 195 *with* RPF 341. (*But see* Text at 65-77 *infra*).

[9] *U.S.* v. *Arnold, Schwinn & Co.*, 388 U.S. 365 (1967).

[10] *U.S.* v. *Topco Associates, Inc.*, 405 U.S. 596 (1972).

1. *The Topco Theories*

The Coca-Cola Company has over the years, by acquisition, integrated forward into the bottling business. Thus complaint counsel assert that the territorial restraints on the distribution of the Coca-Cola brand soft drink were vertical when respondent was simply a supplier of soft drink ingredients, but now that it has acquired bottling facilities, the restraints are horizontal. In addition, when the Coca-Cola Company, while operating its bottling subsidiaries, introduced its allied product lines under licensing agreements which granted exclusive territories to its independent bottlers as well as its own bottling facilities, it allegedly became involved in a "horizontal" market division scheme for the sale of the allied products. (App. Br. 55–56, Amici Br. 13). Amici and complaint counsel contend that geographic market restraints imposed under these circumstances serve no purpose except to stifle competition. Both situations are said to constitute per se illegal horizontal market divisions under the Supreme Court's decision in *Topco.* [8]

a. Acquisition of Bottling Subsidiaries by The Coca-Cola Company

Although The Coca-Cola Company is both a supplier of syrup and a soft drink bottler, the record as a whole demonstrates that the restraints involved here are not primarily "horizontal" within the meaning of the court's *Topco* decision. Admittedly, the line which separates the "vertical" from the "horizontal" forms of a geographic market allocation arrangement is not always as easy to distinguish as the market plane to which they refer might tend to indicate. Both types of restraints at times may, at a given level of production or distribution, exhibit similar competitive characteristics which, on the surface, obscure the firm or firms which are their true source. (*U.S.* v. *Sealy, Inc.*, 388 U.S. 350, 352 (1967)). Consequently, only by ignoring the essential relationships which exist between the respondents and the independent bottlers might it be concluded that the restraints are *Topco*-type "horizontal" market allocations based solely on the fact that respondents operate bottling facilities and are thus potential competitors of the independents, and vice versa.[11] [9]

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[11] Dual-distributing manufacturers and their independent wholesalers obviously can be "in competition with each other" and have so been adjudged in cases which have, for example, construed the scope of the now-repealed Fair Trade Law exemptions to the Sherman and Federal Trade Commission Acts. *See U.S.* v. *McKesson & Robbins, Inc.*, 351 U.S. 305 (1956), *and* Rubbermaid, Inc., F.T.C. Dkt. 8939 [87 F.T.C. 676]. (The Fair Trade Laws were repealed by the

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The Coca-Cola Company's forward integration by acquisition into the bottling industry did not alter in a substantive way either the nature of the restraints or the implementation [10] policies employed by The Coca-Cola Company with respect to established bottling territorial relationships. These restraints were in place nationwide for several years prior to Coca-Cola's entry into bottling.[12] When it

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Consumer Goods Pricing Act, Pub. Law No. 94–145 (Dec. 12, 1975).) Both cases involved resale price maintenance agreements coupled with supplier-imposed customer restrictions.

Notably, the interpretations applied in the fair trade cases cited actually narrowed the fair trade law resale price maintenance immunities. As we noted in *Rubbermaid*, ". . . we will construe strictly any provision which deviates from fundamental antitrust policy, for exemptions from the antitrust law are to be strictly construed. . . ." (Slip Opinion, p. 24, fn. 45).

Two cases traceable to *McKesson* have condemned, as "horizontal," agreements between dual-distributing suppliers and their independent distributors. *See Interphoto Corp.* v. *Minolta Corp.*, 295 F. Supp. 711 (S.D.N.Y. 1969), *aff'd per curiam*, 417 F.2d 621 (2nd Cir. 1969) (resale price maintenance and territorial restrictions), cited in *Hobart Brothers Co.* v. *Malcolm T. Gilliland, Inc.*, 471 F.2d 894 (5th Cir. 1973). In *Hobart*, the supplier of welding equipment competed with its distributor in the sale of the equipment to other customers. The supplier and distributor were also competitors in the manufacture and sale of continuous wire feeder mechanisms. Efforts by the supplier to police its territorial restrictions, through disparagement and finally termination of the welding equipment distributorship, damaged the distributor's business in the sale of both welding equipment and wire feeder mechanisms. (*Id.* at 898, 903). The Fifth Circuit found that the territorial restriction in these circumstances operated horizontally. The court also noted in dicta, however, that agreements limiting the area in which other independent distributors could sell Hobart products in competition with Hobart constituted horizontal territorial allocations. (*Id.* at 899).

In non-fair trade cases, the Supreme Court has not applied the fair trade "in competition" standard in determining horizontality in dual-distribution, territorial restriction situations. Had the standard been applied, for example, in *White Motor* the restraints before the court conceivably could have been treated as horizontal arrangements; Justice Clark, citing *McKesson* in his dissenting opinion, argued as much with respect to White's customer restrictions. In fact, White Motor had reserved to itself the business of selling its trucks to certain types of customers located within the "exclusive" territories it granted to its independent distributors, *White Motor Co.* v. *U.S.*, 372 U.S. 253 (1963). While the per se rule in *Schwinn* has been overruled, the opinion contains useful guidance for purposes of classifying restraints. Notably, Schwinn shipped bicycles directly to retailers, while paying the order-taking distributor a commission on the sales (*Schwinn, supra* at 370), and consequently the situation involved substantial participation by the manufacturer in the bicycle distribution chain. The court stated:

> . . . we are here confronted with challenged vertical restrictions as to territory and dealers. The source of the restriction is the manufacturer. These are not horizontal restraints in which the actors are distributors with or without the manufacturer's participation. (at 372).

Later in *Schwinn* the court again emphasized that it was:

> . . . dealing here with a vertical restraint embodying the unilateral program of a single manufacturer. We are not dealing with a combination of manufacturers . . . or of distributors . . . . We are not dealing with a "division" of territory in the sense of an allocation by and among the distributors . . . or an agreement among distributors to restrict their competition. . . . We are here concerned with a truly vertical arrangement. . . . (at 378, citations omitted).

[12] Territorial monopolies, intrabrand, have been a dominant characteristic of respondents' distribution system since the beginning of the Coca-Cola bottling business. Looking back upon respondents' humble origins, exclusive territories may have, as they contend, been necessary to attract local businessmen to invest in their bottling venture. We certainly ascertain nothing in the record which disputes respondents' characterization of the difficulties encountered by those who labored, nearly three-quarters of a century ago, to solicit investor interest in soft drink bottling.

Prior to 1900, bottled Coca-Cola was virtually unknown. At the time, Coca-Cola syrup was sold almost exclusively through fountain jobbers to retailers who performed the function of mixing the syrup with carbonated water, and the finished soft drinks were served, most often for immediate consumption by the consumer, at the retailer's place of business. The demand for Coca-Cola in containers capable of maintaining its effervescence which could be purchased at the store and taken home for later consumption was, in fact, an outgrowth of the fountain business.

A brief survey of the economic landscape of 1900, as revealed in the record, leads us to conclude that businessmen of that era probably considered soft drink bottling little more than a newfangled invention with a questionable future. Having never before been done to any significant degree, it had virtually no financial track record to guide potential investors. Even the management of The Coca-Cola Company at the time had serious reservations about its feasibility. Coca-Cola bottling was not an innovation of The Coca-Cola Company; rather, it appears from stipulated record evidence that its then-chief executive probably considered the scheme to bottle the product an undertaking more suited to the taste of adventurous speculators than serious investors.

Thus viewed in its historical context, soft drink bottling was a fledgling industry when territorial exclusivity was

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acquired a bottler, The Coca-Cola Company itself became subject to the [11] same territorial limitations it had previously imposed upon the acquired bottler. (Tr. 512–13, 527).[13] With each [12] acquisition, then, The Coca-Cola Company merely replaced an independent bottler within a preexisting distribution scheme.[14] No evidence was introduced that the acquisitions actually changed either the competitive effects of the territorial restrictions or the basic relationships among the bottlers. While it is true that respondents may at times resolve border disputes involving territorial boundaries which occasionally erupt among the bottlers, unlike *Topco*, it has not been established on this record that the independent bottlers exercise control over any respondent or the way in which a respondent implements the territorial aspects of its trademark licensing programs. *See U.S.* v. *Sealy, Inc., supra.* Nor has it been established on this [13] record that the tapestry of Coca-Cola bottling territories is the product of horizontally contrived arrangements among the bottlers actively blessed or passively accepted by any respondent. (*See Fontana Aviation, Inc.* v. *Beech Aircraft Corp.*, 432 F.2d 1080, 1084 (7th Cir. 1970).[15]

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originally awarded to Mr. Thomas and others, and, by them, subsequently in smaller parcels to hundreds of local bottlers. In this way, they attracted the manufacturing and distribution capital to develop a new business and to expand the sale of a new product, finished Coca-Cola in bottles, into new markets. In these circumstances, the language in *White Motor Co.* v. *United States*, 372 U.S. 253 (1963), quoting from Justice Brandeis in *Chicago Board of Trade*, is appropriate:

> The history of the restraint, the evil believed to exist, the reason for adopting the particular remedy, the purpose or end sought to be obtained, are all relevant facts. This is not because a good intention will save an otherwise objectionable regulation or the reverse; but because knowledge of intent may help the court to interpret facts and predict consequences. (at 261).

Evidence concerning the history of respondents' territorial restrictions and the essential relationships which have existed basically unchanged over the years among the respondents and between them and the independent bottlers confirms our conclusion that the restraints on the sale of Coca-Cola are not the offspring of a horizontal conspiracy or collusive horizontal agreements.

[13] The record shows that there are several types of Coke bottler licensees. (CPF 83). Those bottlers which originally acquired the rights to bottle Coke directly from The Coca-Cola Company or its predecessors are known as parent bottlers. This category now includes only the Thomas Company respondents, the other parent bottlers having been acquired by The Coca-Cola Company. The parent bottlers, in turn, parceled out pieces of their territory in which they granted exclusive rights to local investors known as first-line bottlers. (CPF 84). Territorial restrictions were imposed upon each of these first-line bottlers by the parent bottlers. In some instances, first-line bottlers have further carved up their territories and have licensed others, known as "sub-bottlers," to bottle Coca-Cola on an exclusive basis.

[14] This conclusion is corroborated by the fact that The Coca-Cola Company entered Baltimore not as a parent bottler, but as a first-line bottler. It operates within the exclusive territory of the bottler which it acquired, and its parent bottler is a Thomas Company. (App. Br. 23, 55). Furthermore, the record shows that several bottling facilities were acquired by respondent to assure product availability in territories in which the independent bottlers were leaving the market and other independents with sufficient capital and know-how were unavailable to take their place. (Tr. 913, 922).

It should be noted that soft drink syrup producers and particularly small manufacturers may be able to enter new markets nationwide to compete with dominant firms like Coca-Cola and PepsiCo by offering exclusive trademark licenses of limited duration to existing bottlers or by encouraging new bottlers into the market. If the search for independent capital is unsuccessful or if an independent bottler decides to withdraw from the market, a syrup company may then decide to integrate vertically in order to preserve its market position. Should it, in fact, integrate under these circumstances, it would, of course, be entering the "bottling level," but we do not read *Topco* as condemning this type of dual-distribution program as a horizontal market allocation arrangement.

[15] An aggregation of geographic restraints designed by a franchisor for the purpose of eliminating both intrabrand and interbrand competition between itself and its franchisees may, under certain circumstances, result in a "horizontal" allocation of markets. *See American Motor Inns, Inc.* v. *Holiday Inns, Inc.*, 521 F.2d 1230 (3rd Cir. 1975), in which the court concluded that since the franchisor:

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This is not to say that the type of territorial restrictions traditionally considered vertical are devoid of horizontal competitive implications; but on the facts before us, we cannot conclude that the horizontal aspects of these restraints are, for classification purposes, predominant in the *Topco* sense simply because they now prevent intrabrand competition among independents and Coca-Cola's subsidiaries, whereas previously they functioned as a barrier to intrabrand competition only among independents. In the latter situation and in makrets in which respondent Coca-Cola entered the distribution system below the level of a parent bottler, as it did in the Baltimore territory, complaint counsel concede the restraints are vertical (App. Br. 55), and for all that appears in the record, the essential nature of these restraints in instances respecting the distribution of bottled and canned Coca-Cola, despite The Coca-Cola Company's acquisition of parent bottlers, remains vertical.[16] [14]

b. Introduction of New Product Lines by a Dual-Distributing Supplier/Trademark Licensor

The allied products of The Coca-Cola Company, TAB, Sprite, Fresca, Fanta, and Mr. PiBB were developed by respondent, at least in part, to satisfy the demands of its bottlers for additional soft drink flavor lines. These products were first introduced in the early 1960's, long after The Coca-Cola Company had entered the bottling level, and were offered to the integrate bottling operations and the independent Coca-Cola bottlers alike on an exclusive basis for distribution within their existing Coca-Cola bottling territories.[17] Allied product licenses were granted by The Coca-Cola Company directly to the bottler. Unlike many of the Coca-Cola licenses, no parent bottlers are involved in these licenses.[18] Consequently, complaint counsel view the territorial aspects of these allied product licenses as market allocation agreements

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> . . . in one of its capacities, was dealing on the same market level as its franchisees, its contracts that, in effect, foreclose such franchisees from operating either Holiday Inns or non-Holiday Inns in cities where HI operated an inn, except with HI's permission, constituted market allocation agreements among competitors. (at 1254).

Respondents' bottlers, in contrast, are not prevented from manufacturing or distributing soft drinks trademarked by competing syrup companies; nor do respondents have any control over the geographic area in which its bottler may distribute such products.

[16] In *Adolph Coors Company*, 83 F.T.C. 174, the Commission considered, strictly in a vertical context, an aggregation of trade restraints, including price fixing and territorial restrictions, by a brewer which distributed its products through independents and "a wholly-owned subsidiary of respondent." (83 F.T.C. at 175).

[17] *See* Tr. 540–41, CX 104A, CX 110A, CX 115A, 119A, 121A (allied product territories of the Baltimore subsidiary); *and*, for example, CX 199A, CX 202A, CX 206A, CX 207A (allied product territories of the Richmond bottler); CX 256, CX 259A, CX 264A (allied product territories of the Washington bottler); CX 564A, 565A, 566A (allied product territories of the Dover, Delaware bottler). In each instance, the boundaries within which the bottler may produce and distribute the allied product are identical to the territorial boundaries specified in its Coca-Cola license.

[18] The Coca-Cola bottlers were not required to handle the allied products, and many which were already producing soft drinks, made from syrups produced by other syrup companies such as Dr. Pepper or Sunrise flavors, declined the license for certain Fanta flavor lines or Mr. PiBB, Coca-Cola's "Pepper-type" drink.

between potential competitors; specifically, respondent's own bottling subsidiaries and the independent bottlers.

While the allied product licenses are conferred by a manufacturer which also produces and sells finished soft drinks at wholesale to retailers within exclusive territories, absent evidence of collusive activity among the bottlers, we conclude that the introduction of new product lines by a vertically integrated soft drink syrup company using its existing channels of distribution would not, under *White* and its progeny, necessarily render the bottling agreements "horizontal." [15]

Since complaint counsel have the burden of proof, we shall assume that the "allied product" trademark licensing programs for each flavor line were conceived by The Coca-Cola Company, acting unilaterally as the syrup and concentrate supplier and trademark licensor. No evidence to the contrary was introduced. The record as a whole does not evidence any collusion among bottlers concerning the allied product territories or that bottlers jointly participated in or exerted any control over the territorial aspects of respondent's allied products distribution scheme. (*See GTE*, *supra* at 71,901, fn. 28). Rather, the evidence indicates that respondent, alone, elected to distribute the allied products through the existing network of Coca-Cola bottlers using the Coca-Cola-type licensing system.

While not dispositive of its liability in this proceeding, it is also relevant, for purposes of classifying the restraint as horizontal, or vertical, that complaint counsel failed to demonstrate, in any respect, that The Coca-Cola Company's presence at the bottling level substantially altered either the competitive effects of the allied product restrictions or the essentially vertical relationships respondent had with its bottlers before the allied products were introduced. We conclude that *Topco* is not applicable in this context.

2. *Vertical Per Se Theories*

As we mentioned previously, the Supreme Court, in overruling *Schwinn*, has not entirely rejected the possibility that vertical restrictions may, in individual cases, be declared per se unlawful, but it has toughened the standard considerably. Only those restraints found to be "pernicious" and without "any redeeming virtue" now justify per se treatment. The types of competitive situations, other than price fixing, which may meet this standard are unclear, but beyond that, the trier of fact and appellate tribunals must be receptive to the fact that situations may exist in which the imposition of a vertical restraint may, under *GTE*, still be per se unlawful.[19] [16]

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[19] During the pretrial period following issuance of the complaint, complaint counsel's predecessors, citing the Supreme Court's decision in *Schwinn*, filed with the administrative law judge then assigned to the case a motion for

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On the facts before us, we believe the application of a per se rule would be inappropriate. Taking into consideration the competitive dynamics in this industry, there are important unresolved issues in this proceeding concerning whether open intrabrand competition among the bottlers of Coca-Cola and the allied products would adversely affect interbrand competition in the sale of soft drink beverages. The resolution of these issues in this case, we believe, requires a rule of reason analysis. The burden of proof justifying application of a per se standard has not been met on this record. The territorial aspects of these trademark licensing agreements, or those which may be imposed by other firms in this industry, have not been shown to be typically pernicious and without redeeming virtue under the *Northern Pacific*[20] standard, as adopted in *Continental T.V., Inc.* v. *GTE Sylvania, Inc.*, *supra*. We now turn our attention to the record.

III. EFFECTS OF THE TERRITORIAL RESTRICTIONS

A. THE "CORRIDOR AREA"

Although respondents admittedly impose territorial restrictions on virtually all of their bottlers nationwide, at the trial, complaint counsel limited their proof of competitive impact to an area of the country extending from southern Virginia to upstate New York, an area which has been referred to in this proceeding as the "corridor area." Complaint counsel believe the "corridor area" is a microcosm of the soft drink bottling industry as a whole; thus if the restrictions are found to be anticompetitive in this geographic area, the findings can, according to complaint counsel, be applied to the competitive situation nationwide. We believe complaint counsel have met their burden of establishing the validity of the "corridor area" analysis. Respondents' objections to it notwithstanding, the business of bottling soft drinks in the "corridor area" is, in fact, essentially no different from the bottling business in other areas of the country.

The record shows that within the "corridor" there are urban, suburban, and rural bottlers with single-plant and multi-plant operations, large and small bottlers, first-line bottlers, sub-bottlers, and marketing bottlers with no production facilities. Several "corridor area" bottlers distribute within a single territory. Others, through consolidations or acquisitions, have obtained the rights to distribute

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partial summary decision declaring respondents' territorial restrictions per se illegal vertical restraints on the sale of finished soft drink products. The judge denied this motion (*See* Order Denying Motion by Complaint Counsel for Partial Summary Decision, April 5, 1973); interlocutory review of his ruling was not sought; and the case subsequently proceeded to trial, the vertical per se theory having been abandoned. (App. Br. 3, 5 fn. 1). Amici have revived the theory for consideration on appeal.

[20] *See Northern Pacific Railroad Co.* v. *U.S.*, 356 U.S. 1 (1958).

Coca-Cola in two or more territories. The "corridor area" also includes both private and publicly owned bottlers, a bottler-owned canning cooperative, a major bottling and canning subsidiary of The Coca-Cola Company, contract canners, and interbrand competitors. In addition, Coca-Cola bottlers throughout the [17] country may manufacture and distribute, or "piggyback," soft drinks trademarked by competing syrup companies; and in virtually all instances, they use a route or "store-door" delivery system to distribute at wholesale the soft drink products in various package sizes and types which they either bottle themselves or which are produced for them under agency agreements by neighboring bottlers or canners.

While respondents correctly note several perceptible but minor distinctions in the "corridor area" bottling business, those differences are really inconsequential for the purpose of this proceeding. Respondents, for instance, alert us to the fact that the demand for returnable, refillable bottles tends to be higher in other parts of the country than in the "corridor area" where convenience packaging seems to be more popular. (Tr. 1345–46, 2871–72, 2064, 3781, 2368–69). As a packaging alternative, however, refillable bottles are offered in many markets and are an important factor in several bottling territories including within the "corridor area." The record shows that refillables represent 50 percent of the sales of Coca-Cola in bottles and cans in the Richmond territory; 60 percent in Charlottesville; 65 percent in the territory of the Washington, Pa., bottler; 47.9 percent in Westminster, Md.; 41 percent in Dover, De.; and 74 percent in Montross, Va. (RPF 348). Recognizing, then, that the proportion of soft drinks sold in refillables may be greater in other parts of the country, there is ample use of this form of packaging and sufficient investment by the bottlers in refillable bottle inventories or "float" within the "corridor" to safeguard against any significant distortions in our analysis.

Nor are we persuaded by the argument that the "corridor area" is atypical of the nation as a whole merely because territories may tend to be larger and the population ratio of large and small bottlers may vary in other areas of the country. (Tr. 1336–37, 1345, 3266–67). We believe the record provides ample support for complaint counsel's contention that the "corridor area" represents a reasonable cross-section of the bottling firms which operate throughout the country. Setting aside respondents' protestations and references to insignificant distinctions in "corridor area" bottling, we feel that an accurate assessment of the competitive dynamics in the territories of both large and small bottlers and the interrelationships between bottlers which would, absent the territorial restrictions, be likely to result can be made on this record. Respondents called, as defense witnesses, numerous bottlers from Georgia, Iowa, Texas, California, and other locations beyond the "corridor area." Their testimony is remarkably similar to the testimony of the bottlers situated within the [18] "corridor," including their assessments of the competitive effects of the restrictions under present market conditions and their estimation of the likely consequences of a Commission order eliminating the restraints. Under these circumstances, we find no basis for dismissing the "corridor area" as too dissimilar to the rest of the country to support an analysis of the nationwide competitive impact of respondents' trade restraints.

B. SUPPRESSION OF INTRABRAND COMPETITION AMONG RESPONDENTS' BOTTLERS

Respondents acknowledge that territorial restrictions prevent intrabrand competition among their bottlers, but claim this effect is actually procompetitive and necessary in the interest of promoting the overall efficiency and productivity of its bottler network. (Ans. Br. 12–16, 54). Respondents contend, moreover, that the admitted restraint of intrabrand competition is of no concern unless "the restraint is imposed by parties with excessive market power," the "principal indication" of which "is the ability to set the price for a product free from the influence of interbrand competition." (Ans. Br. 45, 47). On this premise they further contend that the evidence does not show that respondents have "unrestricted market power" with respect to price, packaging, or service (Ans. Br. 47), and that evidence concerning market share and profits does not demonstrate that Coca-Cola has "dominant or monopoly power." (Ans. Br. 49). Implicit in this contention is the idea that absent such market power the asserted efficiency and productivity benefits of restrained intrabrand competition will be passed on to the consumer as a result of interbrand competition.

We do not agree that a showing of "dominant or monopoly power" or "unrestricted market power" is necessary before it may be concluded that suppression of intrabrand competition is unreasonable and in violation of Section 5. Respondents and the ALJ cite the decision in *United States* v. *Columbia Pictures Corp.*, 189 F. Supp. 153 (S.D.N.Y 1960), where the court made the following summary of the doctrine of ancillary restraints (*id.* at 178):

> It permits, as reasonable, a restraint which (1) is reasonably necessary to the legitimate primary purpose of the arrangement, and of no broader scope than reasonably necessary; (2) does not unreasonably affect competition in the marketplace; and (3) is not imposed by a party or parties with monopoly power.

Thus, the court did not hold that market power must be demonstrated before a restraint could be held unreasonable under the Sherman Act, but rather held only that the absence of monopoly power was [19] one of several prerequisites before a restraint might be held reasonable. Indeed, in *GTE* the Court indicated that even a less sweeping restraint on intrabrand competition than we have before us here could be found unreasonable without a showing of market power, even though the company imposing the restraint had a small market share and was far removed from the dominant firm in the industry. *GTE, supra* at 71,893.

While the territories in which Coca-Cola and the allied products are sold are not devoid of interbrand competition, nevertheless Coca-Cola and allied product prices have great competitive significance in the marketplace.[21] Moreover, the record amply demonstrates that respondents' territorial restrictions constitute a serious impediment to free market forces and diminish competition in the manufacture, distribution, and sale of several important soft drink product lines. The record also shows that intrabrand competition would invigorate price competition which would be likely to produce lower wholesale prices for Coca-Cola and the allied products. (Tr. 739, 887–889, 992–93, 1568, 2459, 2885). By suppressing the development of intrabrand competition in the sale of these products packaged in bottles and cans, the restrictions have, over the years, distorted the competitive dynamics of the industry, and have disrupted the natural economic forces which would have, in the absence of restraints, caused an evolution in the geographic market boundaries of respondents' bottlers. [20] Before we consider whether these restraints promote interbrand competition and efficiencies in distribution, as respondents contend, we must take a closer look at the intrabrand effects of the restraint.

1. *Intrabrand Syrup Jobbers*

Respondents argued below and again on appeal that Coca-Cola sold by licensed bottlers in bottles, cans, and pre-mix containers is subject to "vigorous" intrabrand competition from post-mix Coca-Cola syrup sold by independent wholesalers for use primarily at soda fountains and in cup vending machines. (RPF 171–72, IDF 133–34). While the bottlers distribute the packaged finished soft drinks within exclusive territories, a syrup jobber is free to sell post-mix syrup in any geographic market in which a demand for the syrup exists to any customer who has a proper use for it. Several independent wholesalers may compete in the sale of post-mix syrup in any given area, including a few bottlers of Coca-Cola who also wholesale the post-mix syrup primarily to the cold drink trade and, like the jobber, may independently decide where and to whom they will distribute it. (RPF 171, Tr. 1941).

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[21] The complaint in this matter defines soft drink products as including non-alcoholic beverages and colas, carbonated and uncarbonated, flavored and non-flavored, sold in bottles and cans, or through pre-mix and post-mix systems, or the like. (Complaint para. 1(h)). Within this broad product market definition, however, there may be a number of relevant submarkets. For example, in *Sulmeyer* v. *The Coca-Cola Company*, 515 F.2d. 835, 848–49 (5th Cir. 1975), the court found that a lemon-lime flavor segment of the soft drink market was a relevant submarket and, further, that all independent bottlers, as urged by The Coca-Cola Company in that case, constituted a relevant market. We note, however, that the trial below explored the implications of these restraints in an exceedingly broad framework which encompassed interbrand competition within the total context of the soft drink industry. The trial did not focus on structural characteristics in various arguably valid submarket categories; nor did it isolate the competitive effects of these restraints within strict submarket contexts. In a light most favorable to respondents, a record of competitive impact was developed in the context of virtually every liquid, except alcoholic beverages, a person may consume. Particular emphasis however, is placed on flavored carbonated soft drink beverages since virtually all of the bottlers tended to place their emphasis on these beverages in describing competitive products which influence their business decisions.

In his initial decision, the judge, without qualification, found that intrabrand competition between jobbers of post-mix syrup and the bottlers of packaged finished soft drinks is indeed "vigorous." Only by ignoring relevant supply and demand factors, including the fact that the bottler sells a packaged product which is frequently purchased by the consumer in quantity and stored at home for later consumption, would this conclusion be sustainable. (*See* Tr. 2384–85, 1684).

The soft drink bottling industry grew out of the business of selling syrup to soda fountain retailers, but it has always been viewed by respondents and the bottlers as a different business. (Res. Ans. Br. 3–5, 10–11; Tr. 1572–73, 3262). *See The Coca-Cola Bottling Co.* v. *The Coca-Cola Co.*, 269 F. 796 (D. Del. 1920)). This is evidenced by a relationship between The Coca-Cola Company and its bottlers predicated on the distinction between syrup sales to retailers who serve soft drinks to consumers for on-premise consumption and the sale of packaged finished soft drinks to retailers who resell it to consumers for home consumption. This distinction is as valid today as it was when respondent Coca-Cola sold its rights to manufacture and distribute bottled Coca-Cola to Messrs. Thomas and Whitehead.

Admittedly, for certain types of soft drink retailers, there is a viable option to purchase either finished packaged soft drinks from a bottler or post-mix syrup which they can mix with carbonated water just as a bottler would, but the choice is really available only to retailers, such as restaurants, fast-food retailers, cafeterias, sports stadiums, and [21] other types of outlets which serve Coca-Cola in cups, bottles, or cans for immediate consumption. (Stip. No. 3, CX 1244–1). Competing for these accounts against the Coca-Cola post-mix wholesaler, however, a bottler is at a serious disadvantage precisely because he is selling a finished packaged product.

Unlike the bottling and canning of Coca-Cola and other soft drinks, post-mix wholesalers are not required to perform any of the manufacturing functions a bottler performs. Nor is the wholesaler required to provide any dispensing equipment or service and often he does not perform any delivery functions since the post-mix syrup is frequently drop-shipped by The Coca-Cola Company directly to the retail customer.

The record further shows that fountain syrup is often incidental to the bottlers' overall business to the point that they make no effort to sell it. Mr. Navarre, Chairman of the Boards of the Coca-Cola Bottling Co. of Miami, the Delaware Coca-Cola Bottling Co., and the Coca-Cola Bottling Works of Havre de Grace, Maryland, testified about the fountain syrup business:

> Q. — I believe you stated that you don't sell fountain syrup — why have you elected not to? Is there a contractual part of your doing so?
> A. No, sir, it is a competitive situation and ability to be able to furnish to these dealers at this price and the profit contribution under our form of doing business is not sufficient to interest me. (Tr. 1554–55).

Conversely, in selling to other types of outlets, such as retail food stores which cater to a substantial market for Coca-Cola and the allied products in take-home packages, the bottler need fear no intrabrand competition from any of the post-mix wholesalers. This comports with the basic rationale of the soft drink bottling industry. (*See* Tr. 4080–81). In fact, the entire bottling industry exists because of its ability to service the demand for soft drinks in take-home packages which the fountain syrup wholesalers have never been able to reach. (*See* Tr. 1457). Consequently, in the sale of soft drinks in bottles and cans for home consumption, which the bottler alone is uniquely equipped to serve, intrabrand competition from post-mix wholesalers is virtually nonexistent. Mr. Navarre's testimony amply demonstrates that the intrabrand competition which may exist between syrup jobbers and bottlers is confined to a limited, rather well-defined class of customers who cater to the cold drink market, and even as limited, there will be competition between bottlers and jobbers only if the bottler elects to expand into the cold drink trade. Thus a bottler may, in some instances, actively solicit cold drink accounts, but jobbers are, by the nature of their product, foreclosed from competing for bottlers' take-home business. [22] Contrary to the judge's finding, then, it is evident there is virtually no direct competition between syrup jobbers and bottlers for the bulk of the bottlers' business to their traditional food store and other accounts which serve the consumer demand for Coca-Cola, TAB, Sprite, Fresca, and other allied products in take-home packages.

2. *Territorial Restrictions Prevent Procompetitive Geographic Market Expansion and Eliminate Potential Competition*

Complaint counsel contend that respondents' territorial restrictions, rather than fostering greater efficiency, actually deter progress and the efficiency of the bottlers because they prevent the type of production and sales expansion which would enable bottlers to achieve maximum scale economies and further prohibit or discourage the bottlers from taking maximum advantage of improved production, distribution, transportation, and communications systems developed in the last five decades or so. (App. Br. 57). Respondents vigorously dispute each of these contentions. In their view, bottlers large and small have been able to adapt to changing economic conditions, to expand their sales within their territories, and to employ innovative techniques of marketing and packaging. (Ans. Br. 81).

Respondents are correct in their assertion that many of the adaptable technological breakthroughs of the 20th century have not bypassed the bottling industry. Bottling territories were originally parceled out at a time when bottling facilities used manual equipment and finished soft drink products were delivered in horse-drawn wagons over dirt roads. (Tr. 681, 1656–59). Today, in contrast, even the small bottler uses modern delivery trucks (RPF 292), and unlike his predecessor, he operates on a much more efficient production-line basis, using automated equipment which cleanses containers and purifies and carbonates water. He has mechanized systems which mix the syrup and water, fill and cap the bottles, and package the filled containers at varying speeds depending upon the bottle size and the type of bottling equipment used.

These modern automated production lines have, in addition, increased the potential production capacities of both large and small bottlers. At present, soft drink bottlers often produce and distribute, or "piggyback," the soft drinks trademarked by several syrup companies and may, at times, distribute these brands in exclusive territories of various sizes assigned to them by different syrup companies. (*See* Tr. 3078, 3063–65, 3067, 3236). Some Coca-Cola bottlers are also capable of supplying, in addition to the soft drink requirements within their own territories, the requirements of other Coca-Cola bottlers who have retained a territorial monopoly for the distribution of Coca-Cola but have temporarily discontinued producing it themselves (Tr. 529–30, 555, 788–89); other bottlers have entered **[23]** into agency arrangements to supply neighboring bottlers with their requirements for certain package sizes[22] or have, by consolidations and mergers, combined their territories, efficiently serving from one production center an area previously serviced by two separate bottling facilities.

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[22] The small Pepsi bottler in Dyersburg, Tennessee, also piggybacks Dr. Pepper and Bubble-Up and, working

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Originally, the bottlers' territories probably represented a rather close approximation of the geographic boundaries which would have existed in the industry if natural economic forces were left unrestrained. While territories were granted in various sizes and shapes, they probably encompassed an area roughly measured by the distance a turn-of-the-century vehicle could travel in one day. (Tr. 681). Given the technological and transportation limitations of the late 19th and early 20th centuries, under which the original bottlers operated, it seems reasonable to conclude that most territories probably covered an area not significantly smaller than the Coke bottler was capable of servicing efficiently and effectively. As time passed, however, the potential for direct competition among respondents' bottlers grew as automated production of soft drinks replaced manual bottling lines, as new types of packaging were introduced, and as truck transport and road surfaces improved. Despite these advancements, however, respondents' territorial system stands impervious to natural geographic market evolution and procompetitive market extension by independent bottlers.

3. *Territorial Restrictions Indirectly Lessen Competition in the Delivery Services Bottlers Offer to Their Customers*

The record also shows that the restrictions impede the bottlers' ability to respond to the demand for competing delivery services. Since the beginning of the Coca-Cola bottling business, the bottlers have used, almost exclusively, a route-delivery system (or store-door delivery as the bottlers refer to it) which entails frequent, direct delivery by the bottler to each of the customer's retail outlets. In the early days of this business before the chain store, central warehouse era of the 1930s and [24] the introduction of nonrefillable containers in the mid 1950s[23] there may have been few competitive alternatives to store-door delivery. Today, as a result of soft drink packaging innovations improvements in transportation, and the widespread use of central warehouse facilities by retailers and independent wholesalers, there is a market for service options, such as central warehouse

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overtime, was still able to supply larger bottlers, including the large Memphis Dr. Pepper bottler, a subsidiary of RKO, with Dr. Pepper in 32-ounce returnable bottles for ten months. Similarly, the Coke bottler in Las Cruces, New Mexico, supplied the Coke bottler in San Antonio with 64-ounce nonreturnable bottles of Coca-Cola for a period of four months (RPF 258; Tr. 2483-84, 2511-12), and the small Northern Neck, Va., Coca-Cola Bottling Co. supplied Coca-Cola in 32-ounce returnable bottles to other bottlers, including the large Crass organization in Richmond. (Tr. 1635-36).

[23] Pressure from competitive packages forced The Coca-Cola Company in 1955 to abandon its single-package (6 1/2 oz. returnable, refillable bottle) philosophy and authorize the bottlers to use various size refillable bottles and nonrefillable bottles and cans. (Tr. 714, 1344).

delivery and plant pick-up by central warehouse and other customers and respondents' bottlers have the capacity to exploit it.[24] Yet, notwithstanding the demand for these competitive delivery services, a bottler may not, consistent with respondents territorial policy, ship to central warehouses or allow plant pick-up in instances which will result in distribution of the product by the customer outside the bottler's territory. (RPF 49).

While the bottlers who appeared at the trial testified that they prefer store-door delivery to central warehouse delivery because it promotes deep market penetration and allows them to maintain some measure of control over the way the product is merchandised by the retailer on the retail shelves (*See also* RPF 49), it also appears that store-door delivery is preferred today by many bottlers, at least in part, because it is completely compatible with the preservation of exclusive **[25]** territories. (Tr. 1901.[25] In fact, respondents and the bottlers concede not only a strong market demand for central warehouse delivery and plant pick-up by central warehouse customers (RPF 88–90), but also that some bottlers would **[26]** provide a competitive response to this demand were they free to do so. (Ans. Br. 55).[26] Consequently, by hindering central warehouse and plant pick-up

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[24] Central warehousing involves the purchase of soft drinks by the warehouser directly from a bottler or canner for delivery into the purchaser's warehouse. Subsequently, redelivery of the soft drinks is made in the warehouser's own trucks to the warehouser's retail outlets. Warehousers may themselves be retailers (such as large chain supermarkets) who buy for redelivery to their own outlets in their own trucks, or independents who buy for redelivery to non-affiliated outlets or retailer warehouses.

Although the agreements between respondents and the bottlers do not directly prohibit warehouse delivery, respondents concede that the bottlers may not sell Coca-Cola and the allied products to central warehouse customers or allow plant pick-up where the result would be redistribution of these products outside the selling bottler's territory. (RPF 47–49). As a consequence, respondents' territorial policy has indirectly but effectively blocked the development of these alternative modes of delivery.

[25] Respondents and complaint counsel have joined issue over the comparative efficiencies of warehouse delivery and route delivery. A study of both methods of distribution prepared by respondents' expert, Mr. Cowart, shows that the average costs of delivering soft drinks packaged in nonreturnable bottles and cans are approximately the same for route delivery or warehouse delivery. Mr. Cowart's testimony indicates, for example, that the average cost of delivering 32–ounce nonreturnable bottles through warehouses would be 9.6 cents more per case than the cost of current store-door delivery. (Tr. 3438–39). A case of cans is an ideal package for central warehousing because cans are a compact, low-cubage container. Here average costs vary from 3–5 cents in favor of the warehouse in different parts of the country; and if merchandising the product is included in the cost, the warehouse advantage would decline to an average of about .06 cents. (Tr. 3361–62, 3348; RPF 319).

While we cannot conclude on the basis of a study of average costs that central warehousing for soft drink products is more efficient than store-door delivery in all cases, neither is such a study indicative of actual costs in individual competitive situations involving different warehouses, bottlers, and package types and sizes. Route delivery may at times be more efficient than central warehousing for the distribution of large-volume containers such as the 64-ounce bottle; at times it may be a less-efficient method of distribution for soft drinks packaged, for example, in cans. In some instances, then, territorial restrictions may tend to rigidify delivery inefficiencies which a bottler free of the restraint may avoid.

Of course, the complaint in this matter does not challenge route delivery as a method of distribution under any circumstances, including those in which its efficiency is suspect. We are concerned only with the practice of restricting territories, a secondary, indirect effect of which is to inhibit the bottlers from freely competing with respect to the delivery services they may offer depending upon the competitive situation and their own assessment of how best to respond to it. (*See* Tr. 2786–87, *Compare* Tr. 3497–98 *with* Tr. 3532).

[26] It has been suggested that the store-door method of product delivery is inconvenient for some of the bottlers' customers. *See Tomac, Inc.* v. *Coca-Cola Co.*, 1976–2 Trade Cases, ¶60,988 at 69,381–82. However, there is more at stake here than the convenience of some customers. In *U.S.* v. *Aluminum Co. of America*, 148 F.2d 416 (2nd Cir. 1945), Chief

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delivery, territorial restrictions impede the development of an important aspect of competition in the types of delivery services bottlers would offer to their customers in advantageous competitive situations.[27]

4. *Territorial Restrictions Deprive Retailers and Consumers of the Benefits of Open Intrabrand Competition*

Complaint counsel introduced into the record as part of their case-in-chief evidence which shows that the bottlers are not always able to adapt to changing economic conditions and improved technology in marketing and production to achieve efficiencies, especially if their initiatives are inconsistent with respondents' territorial policy. At the same time, the evidence shows that the restriction prevents any intrabrand [27] competition, including price competition[28], in the sale of [28] Coca-Cola and allied products in bottles and cans. As a consequence, respondents' restrictions are, as alleged in the complaint, depriving retailers and consumers of the opportunity to purchase Coca-Cola and the allied products in bottles and cans in unrestricted markets at openly competitive prices. Moreover, these restrictions have repressed the freedom of independent bottlers to expand their businesses or to seize opportunities they may perceive to increase their

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Judge Hand, commenting on the purposes of the Sherman Act, noted:

> . . .that the spur of constant (competitive) stress is necessary to counteract the inevitable disposition to let well enough alone . . . that competitors, versed in the craft as no consumer can be, will be quick to detect opportunities for savings and new shifts in production, and be eager to profit by them.

As the record in this proceeding indicates, at times respondents' territorial restrictions may necessitate a more costly and less competitive method of delivery than those which may evolve in an open market.

[27] As we observed in *Coors*, in a competitive free enterprise system, the decision to exploit the advantages of route delivery or central warehouse delivery:

> . . . should be left to the free, unimpeded play of market forces and the respective, independently exercised judgments of the relevant units of distribution. (at 202).

[28] That the restraint has severe adverse effects on price competition is abundantly demonstrated in the testimony of James Wimberly, Vice President of Coca-Cola U.S.A. In response to Judge Dufresne's questions, he testified that:

> . . . the experiences that I recall, sir, would only result when maybe one bottler raised his price and an adjoining bottler did not at that point in time, and customers or dealers would try to bring Coca-Cola from one territory to the other.
>
> Judge Dufresne: The fellow who raised his price reported to you?
>
> The Witness: Yes, sir, sometimes, that is right, they did.
>
> Judge Dufresne: And what did you do about it?
>
> The Witness: I generally said two things: One is if we do anything about it we have got to be sure that it occurred, and that we are dealing with facts; and, secondly, on some occasions I went to the bottler in whose territory it was reported the merchandise was coming from to try to get him to talk to their dealers or salesman to persuade them not to do that.
>
> Judge Dufresne: Suppose he says, Mr. Wimberly, I don't care what you say. I am going to sell this Coca-Cola to anybody who comes to my door and says, I don't want to pay Charley's prices in the next territory?
>
> The Witness: Well, yes, sir, but you see, most of the time the bottler who allegedly was purportedly involved in that, that one whose territory that the Coca-Cola was coming from, in most instances he was eager not to continue that sort of practice either because he felt pretty sure if he did, the other Coca-Cola bottler was going to try to do the same thing in his territory, and it would just lead to —
>
> Judge Dufresne: He could be persuaded to discontinue it. Is that what you are saying?
>
> The Witness: In most instances they realized that that would lead to great trouble and bickering and fighting between them and were pretty anxious to discontinue —. (Tr. 887–89).

output of Coca-Cola and the allied products by selling these products where and to whom they choose in markets governed by natural economic forces.

IV. CONSIDERATION OF RESPONDENTS' ARGUMENTS SUPPORTING THE ELIMINATION OF INTRABRAND COMPETITION

In concluding that the type of transaction, *i.e.*, sale or consignment, a manufacturer uses to distribute a product "is not sufficient to justify the application of a per se rule in one situation and a rule of reason in the other," the *GTE* court noted that post-sale vertical restrictions may not always be without redeeming virtues. For example, the Court pointed out that vertical restrictions may promote interbrand competition by inducing capital investment and promotional and service activities by the supplier's customers, by increasing marketing efficiency, and by improving quality control. (*See GTE* at 71,900–901). While the Supreme Court did not indicate that lower courts should afford such inducements and efficiency factors dispositive weight, its opinion clearly makes the consideration of these issues relevant in determining whether the restraints are reasonable.

A. CAPITAL INVESTMENT

Respondents contend that territorial restrictions promote the business purposes of The Coca-Cola Company because the soft drink industry is capital intensive and the restraint creates a climate conducive to capital investment. While it is true, as respondents contend, that exclusive territories provide bottlers with a measure of certainty with respect to their ability to recover their investments (RPF 73), we are unable to conclude, on this record, that a free market would otherwise render the bottlers incapable of operating at a profit.

The fact that the risks which attend a bottler's efforts to recover his investment would increase without territorial intrabrand monopoly protection is simply a corollary to the conclusion that as competition intensifies, business risks of capital recovery increase to the entrepreneur. While capital investment considerations, as we have previously noted, may justify a territorial restriction imposed by a new entrant or a failing or faltering firm, we do not, in [29] applying Section 5, ordinarily distinguish between capital-intensive and less capital-intensive businesses by applying different antitrust standards to them, granting the former license to restrain trade because it promotes capital investment while mandating, in the case of the latter, that competition should be preserved. (*Compare Tomac, supra* at 69,381). In competitive markets, prices may be expected to reflect the capital requirements of the firms in the industry in addition to providing entrepreneurs a fair return on their investments.[29]

Shielded by artificial trade barriers created by The Coca-Cola Co., bottlers may well feel secure in making investments which might seem unwise to them if their decisions were being fashioned by free market demands; but this is further evidence of the significant degree to which competition may be lessened by these restraints. Here territorial restrictions are not serving the interests of competition in aid of an aspiring new entrant or a failing or faltering firm which cannot otherwise find investors to put up the distribution capital necessary to market its product. In this instance, the restraint is reducing the entrepreneurial risk of investment by lessening competition among the firms which wholesale one of the most **[30]** popular consumer product lines in American industry. (Tr. 685).[30] While intrabrand competition may reduce the profit in bottling Coca-Cola and allied products, respondents' failed to establish that these prized trademarks and premium products would not still remain viable interbrand competitive factors in an open, unrestricted marketplace. As such, we cannot sanction anticompetitive conduct for the purpose of allowing respondents' bottlers to continue, in perpetuity, to make capital-investment decisions in response to the distorted economic forces within their exclusive territories.

B. AVAILABILITY AND MARKET PENETRATION

By using route delivery in exclusive territories, the bottlers have maximized their market penetration and the availability of Coca-Cola, putting it in every conceivable location a soft drink may be sold and placing it within "arm's-reach of desire." (Tr. 696). Numerous bottlers testified that deep market penetration and product availability are crucial to selling soft drinks in bottles and cans successfully. (RPF 77). This marketing philosophy has led the bottlers to service large numbers of vending machine accounts, small outlets, and "special events" which they claim are unprofitable. (RPF 83). Many of the bottlers who engage in these types of unprofitable activities do so, they say, to obtain "paid sampling" of their products "to get the product awareness to make the larger accounts profitable. It is a matter of developing a market, training people to drink Coca-Cola." (Tr. 1454). In the opinion of the President of The Coca-Cola Company, territorial restrictions encourage this type of market penetration because "(t)he fellow who has a limited field to till obviously has to till it better in order to get the most out of it." (Tr. 696, RPF 84).

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[29] Evidence of the profit bottlers realize on the sale of Coca-Cola or the allied products is in a state of disarray. To begin with, profit is variously described by different bottlers as dividends on book value or as a return (1) on sales, (2) on book value, (3) on investment, (4) on invested capital (5) after taxes on the replacement value of investment, (6) on the market value of investment, and (7) on equity. For all that appears in the record, each bottler may calculate profits on a different basis. Moreover, seven of the ten witnesses, relied upon by respondents in support of their contention that the profit levels of their bottlers are reasonable (RPF 266), piggyback brands other than Coca-Cola and the allied products. Profit on the sale of Coca-Cola products by these bottlers is not indicated. There is, as a consequence, little basis for a comparison of the profitability of Coca-Cola bottling with other industries; nor do we find support for the conclusion that the return obtained by bottlers on the sale of Coca-Cola and allied products is not "abnormal" when compared with other industries. (RPF 265). Furthermore, the profitability of respondents is not reflected in the record.

If respondent were a new entrant or a failing or faltering firm, profitability might be a relevant consideration in assessing these restrictions. However, we find it difficult to justify the restraint, in this instance, as a means of improving respondents' profits or those of its bottlers.

[30] Evidence in the record indicates that Coca-Cola bottlers are firmly entrenched in the fabric of the bottling industry and that their Coca-Cola brand alone is often a leading brand in their territories. This is reflected in a stipulated survey of 36 cities, from Maine to California, in which Coca-Cola, as a single brand, consistently ranked among the top four brands in each city. (RX-2Y-Z38, *See* Tr. 2691).

The record does not indicate whether The Coca-Cola Company consistently sells syrup unprofitably to some of its bottlers as its bottlers sell unprofitably to a large number of accounts presumably to create a demand for Coca-Cola; but it would not be second-guessing the bottlers' business judgments to observe that The Coca-Cola Company may be "free riding" on the volume generated by its independent bottlers' give-aways and unprofitable sales. The Coca-Cola Company, in selling the syrup and [31] concentrate soft drink ingredients to its bottlers, profits by the expanded sales universe of its bottlers, even if that universe includes accounts which are unprofitable to the bottlers.[31]

At the same time, a bottler typically charges a uniform or level price to all of his customers irrespective of the fact that price differences between customers may be justified on the basis of different delivery costs the bottler incurs in serving each outlet. Consequently, some accounts which may cost the bottler less to service probably contribute a disproportionately higher share of the overall cost of the bottler's market penetration. (Tr. 4043). And eventually, those retailers who may be paying or "subsidizing" part of the costs associated with deliveries to other retailers will pass on to consumers, in the form of higher prices, any added cost they may be absorbing. (Tr. 4042). [32]

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[31] The Court in *GTE* noted that vertical restrictions may increase economic efficiency because the manufacturer desires to minimize his cost of distribution and to encourage dealers to sell at "the lowest retail price possible * * * because a lower retail price means increased sales and higher manufacturer revenues." 1977-1 Trade Cas. Para. 61,488 at 71,901, n. 24, citing Note, 88 *Harv. L. Rev.* 636, 641 (1975).

The trademark license to bottle and sell Coca-Cola contains a fixed syrup price which can change only in accordance with a formula tied to the price of sugar. (CX 9A-G, CX 11A-B, CX 13A-B). Hence, The Coca-Cola Company can raise its syrup price vis-a-vis bottlers only when sugar prices rise. The fixed syrup price means that The Coca-Cola Company cannot profit from higher prices charged by bottlers for Coca-Cola. Only more syrup volume produces more profit. (Supplemental Br. of Intervenors Coca-Cola Bottling Co. of L.A., *et al.*, at 6). It is not possible on this record to state definitely whether the bottlers' market penetration in exclusive territories generates greater syrup and concentrate volume and profit for The Coca-Cola Company than would intrabrand competition among bottlers, but the latter probably would, in many instances, result in lower wholesale prices for the finished soft drinks.

It should be noted that several witnesses testified that while wholesale prices in open markets would probably be lower for some customers, they might be higher for other customers. As we noted in *Boise Cascade Corp.*, Dkt. 8958, issued January 11, 1978 [91 F.T.C. 1]:

> By "lower" (prices) we do not mean simply lower for all customers. Elimination of restraints of trade may result in *raising* prices to some purchasers (perhaps those whom it is costlier to supply) while lowering them to others. In a freight intensive industry the reallocation might occur roughly along lines of relative actual freight costs. (at 6 fn. 4).

The testimony in this proceeding reflecting the likelihood that prices might rise for some customers and be lower for others absent the restraint is consistent with our observation in *Boise* about the workings of a competitive market. In this instance, the free market would be likely to provide those retailers who are efficient not only the opportunity to buy Coca-Cola and allied products from competing bottlers at prices which more accurately reflect costs but also the option to pass on to consumers the benefits of their efficiency.

We acknowledge that the elimination of exclusive territories may force the bottlers to abandon their level pricing policies and begin to charge prices which reflect the actual cost differences in servicing various retailers. A bottler who elects to compete for accounts in neighboring territories or who is forced to defend against the forays of intraband rivals which seek the business of his previously captive outlets will no doubt lose the leverage of intrabrand monopoly to extract a price from some retailers which reflects the cost of market penetration to other retailers. Consequently, if the degree of market penetration respondents now enjoy fails to reflect actual costs of servicing each customer, it is likely that some adjustments will be necessary: level pricing may give way to pricing which more closely approximates costs, or bottlers may establish a minimum volume which they will deliver to customers, or they may encourage plant pick-up by customers who cannot be serviced efficiently. But the marketplace would benefit from the increased competition, and we cannot conclude that respondents' interests in maintaining the status quo supercedes this consideration.

C. ADVERTISING AT THE LOCAL LEVEL

Respondents also contend that a bottler's interest in advertising and promoting Coca-Cola at the local level will subside if another bottler selling the same brand can take advantage of his efforts. Exclusive territories prevent this type of "free riding," and thus encourage Coca-Cola's promotion at the local level.

Recently, the court in *GTE* noted that the extent to which vertical restraints on intrabrand competition alleviate market imperfections such as the "free rider" effect and promote interbrand competition may be a relevant consideration in assessing the reasonableness of a vertical restriction. Further guidance on this issue was provided in *Bates* v. *State of Arizona*, 433 U.S. 350, 1977-2 Trade Cases, ¶ 61,573. In *Bates* the court observed that where consumers have the benefit of price advertising, retail prices often are dramatically lower than they would be without advertising." (at 72,330). The court further noted in *Bates* that advertising may facilitate entry by a newcomer seeking to penetrate the market. (at 72,331). Under certain circumstances, price advertising, brand enhancement or image advertising by a new entrant, for example, and advertising which informs consumers about distinct product attributes may, to a greater or lesser [33] degree, enhance the competitive vigor of a market.[32] In this instance, however, the burden of the restraint exceeds the benefits of the advertising it is said to encourage. After 75 years of advertising by respondents and the bottlers, the record clearly shows that it is intrabrand competition which is likely to produce the pressure necessary to reduce the wholesale price of Coca-Cola.[33] (*See* text at 51–54 *infra*).

Unlike *GTE* and *Bates*, which involved advertising by those who offered goods or services to ultimate consumers, respondents' bottlers usually sell their products to retailers. As wholesalers, the bottlers admittedly have no control over retail prices charged by their customers. In contrast, Sylvania's retail dealers, like the lawyers in Arizona in the *Bates* case, advertise prices to their immediate customers. [34] Between the bottlers and consumers, however, an additional independent retail level of distribution usually intervenes. (*Compare* RPF 218 *with* Tr. 2496). Consequently, bottlers may only suggest retail prices, and while this may indirectly influence the retailers' pricing decisions, we do not consider suggested price advertising a substitute for intrabrand competition at the wholesale level which results in lower wholesale prices and, in turn, competition among retailers which results in lower retail prices. (*Compare* RX 5, RX 56, 58–61, *and* RX 101 (advertising by bottlers, Tr. 1982–83, 2493, 2497, 3031) *with* RX 57A–57Z, (advertising by retailers, Tr. 2496). As the court observed in *Bates:* "advertising is the traditional mechanism in a free-market economy for a supplier to inform a potential purchaser of the availability and terms of the exchange." (at 72,330). The record, in this instance, leaves little doubt that the bottlers would have every incentive to price promote their products in competition with intrabrand bottlers and to convey information relating to the terms of sale or the competitive packaging or service alternatives they may offer to their potential purchasers, the soft drink retailer. (*See* RX 62, Tr. 2500). In fact, the amount of such information received by the potential customers of competing intrabrand bottlers would probably increase. The free rider problem is not likely, for example, to prevent a Coca-Cola bottler from advertising to retailers that his price is lower than that of his intrabrand competitors or that he offers them various delivery options or credit terms. Nor can we conceive of any reason why retailers who purchase their soft drink supplies from competing intrabrand bottlers would lack the incentive to convey similar information to their customers, the ultimate consumer.[34] [35]

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[32] It has been argued that territorial restrictions cure the "free rider" problem, and thereby promote advertising and merchandising efficiencies at the local level. It is not inconceivable, however, that the pressure of intrabrand competition might encourage bottlers to increase their overall efficiency by cutting costs associated with advertising and merchandising beyond that which the free market might demand. (*See Bates*, *supra* at 72,331, fn. 35).

[33] In this instance, we recognize that intrabrand competition may well have an effect on the types of merchandising and advertising a bottler may elect to provide to his customers in response to the types of merchandising efforts customers and consumers demand from the bottler. Presumably some customers would elect to purchase from a bottler offering lower prices and fewer merchandising services if a choice between lower price or increased merchandising were available. Conversely, in exclusive territories a bottler arguably gains a "free ride" on consumers who may end up paying for any excessive advertising, merchandising, or local sales efforts which would be discouraged in favor of price competition. As the Supreme Court observed in *Northern Pacific Ry. Co.* v. *U.S.*, *supra*, the antitrust laws rest:

> . . . on the premise that the unrestrained interaction of competitive forces will yield the best allocation of our economic resources, the lowest prices, the highest quality and the greatest material progress, while at the same time providing an environment conducive to the preservation of our democratic political and social institutions. But even were the premise open to question, the policy unequivocally laid down by the Act is competition.

Thus, the potential efficiency-creating aspects of a practice which substantially diminishes competition cannot, on alleged efficiency grounds alone, always be justified under Section 5 of the Federal Trade Commission Act.

Although bottlers may be reluctant, absent territorial exclusivity, to engage in brand enhancement or image advertising which may be especially susceptible to same-brand free riders, it is highly unlikely that consumer recognition of the Coca-Cola and allied produce brands would fade appreciably as a consequence. The Coca-Cola Company, an established giant in the industry, has not shown itself to be in need of financial assistance to promote these brands. Unlike the situation in *Sandura Co.* v. *F.T.C.*, 339 F.2d 847, 854, 858 (6th Cir., 1964), this record does not show that The Coca-Cola Company must depend upon its bottlers for funds to sponsor national, regional, and local level advertising. This, then, is not a case in which the restraint is promoting interbrand competition by aiding a new firm to enter the soft drink industry or by helping to forestall the exit of a failing or faltering firm as in *Sandura*. According to its President, Coca-Cola: ". . . is the most widely recognized name in American commerce and indeed in world commerce . . . it has huge value." (Tr. 685). We conclude, in this instance, that advertising-related considerations which may justify the restraint in the interest of fostering interbrand competition by new or faltering firms do not apply here.

D. QUALITY CONTROL

Respondents contend that territorial restrictions promote product quality in essentially two ways. Because a bottler has a limited geographic area, respondents submit that he cannot afford to risk losing customers who become dissatified with the quality of his product. The restrictions presumably induce bottlers to manufacture a high-quality product and then to ensure that it is subsequently stored and merchandised in a way which prevents the buildup of stale inventory at retail outlets. (RPF 126, Tr. 762, 699). Respondents also contend that the restrictions enable them to monitor, at the retail level, the quality of the product produced by each bottler.

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[34] Of course, advertising by bottlers may sometimes convey information useful to consumers. For example, an ad in the "San Antonio Light" sponsored by the San Antonio, Texas, Coca-Cola bottler on December 3, 1970, which discussed the merits of refillable bottles may have been useful to some consumers. (RX 60, *Compare* Tr. 2915). It is in this regard relevant, however, that consumer organizations have filed a brief as amici urging the Commission to lift the territorial restriction despite the advertising "free rider" problem. (*See Bates*, *supra*, at 72,331 fn. 35). Moreover, advertising is discretionary even by a bottler protected by territorial restrictions. He may choose not to advertise at all or he may direct his advertising to product attributes with which consumers are generally familiar (Tr. 2915) or that consumers may learn about, without incurring significant search costs, through advertising by The Coca-Cola Co. or by retailers or from other sources in the marketplace. Thus the value to consumers of advertising by the bottlers is highly speculative. We are, therefore, unable to conclude that advertising by bottlers which may on occasion convey information potentially useful to comparative shoppers (*see* RX 60; Tr. 2499; *see also* RX 56, 61 and 101), out-weighs the sacrifice of intrabrand competition, in perpetuity.

1. *In Manufacturing*

To ensure that bottlers are properly preparing the finished soft drink products, The Coca-Cola Company has a Quality Control Department which inspects, on an average of three to four times a year, every bottling and canning facility which manufactures Coca-Cola and allied products. Its inspections are generally unscheduled and unannounced and include water analysis, bacterio-logical checks on water and processing equipment, bottle washing solution checks, sanitation monitoring, and finished product syrup content and degree of carbonation. In addition, each production facility is required monthly to submit product samples for analysis by respondent Coca-Cola's quality control lab. (RPF 121). In this way, The Coca-Cola Company frequently and routinely monitors the bottlers' manufacturing process to ensure that they are producing soft drinks in accordance with its standards of quality. (*See* Tr. 2669). Contrary to respondents' contentions, however, there is really no connection between these types of quality control inspections and the areas where independent bottlers sell the finished product; plant facilities can be inspected regardless of where the product is eventually sold. [36]

Furthermore, even though the bottlers presently operate within exclusive territories, the possibility is ever present that a bottler, despite his intrabrand monopoly, may be tempted for short-term profits or other reasons to cut corners by, for example, reducing the amount of syrup he mixes with carbonated water to produce the finished product, thereby reducing its quality.[35] Recognizing this,

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[35] Respondents' quality control inspectors also spot-check their bottlers by obtaining, for analysis, products which they purchase directly from retailers. (Tr. 921, 974–75). Because the bottlers presently need not identify themselves on their packages, successful spot checking now depends, in large measure, on the assumption, validated by respondents' territorial policies, that the soft drinks found on the retail shelves within a given territory were sold to the retailer by the bottler in that territory. To this extent, territorial restrictions facilitate product-source identification.

Yet the issue of whether territorial restrictions could ever be justified on the ground that they indirectly encourage quality control by assisting respondents' monitoring efforts need not be decided here. Rather, we find that respondent could as easily continue spot-check, quality control inspections at the retail level by requiring each bottler to place an identification mark on his product. Obviously, neither marking requirements nor territorial restrictions provide fool-proof safeguards against the production and distribution of defective products (RPF 125) or the "midnight" batch of substandard products which a bottler could presumably intentionally produce. A cheating bottler could be difficult to trace under either monitoring mechanism, yet a simple product-source identification mark (Tr. 804) like dating codes which bottlers may now employ (Tr. 1116–1119) would allow respondents to determine product

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respondents have provided the bottlers with the added business incentive not to produce substandard soft drinks. They have conditioned each bottler's right to continue to produce the trademarked product upon his faithful adherence to their quality standards. (Tr. 911–12). Thus a bottler's failure to meet respondents' standards of quality may result in the cancellation of his trademark license. (Tr. 778). At the manufacturing level, then, unscheduled plant inspections and frequent product sampling, coupled with the threat of termination, if not the act itself, should provide a strong deterrent to the bottler who might be inclined to cheat on quality, notwithstanding the markets in which he may ultimately distribute the finished products. [37]

2. *In Distribution*

Respondents further point out that their trademarks appear on the finished products which reach consumers, so their interest in maintaining product quality extends to the retail level. Respondents note that the bottlers assist in their overall quality control effort by offering stock rotation services to retailers and by removing the old product which may have deteriorated on the retail shelves.

The Commission recognizes the interest of a supplier in maintaining the quality of a trademarked product in the channels of distribution through which it travels to the marketplace. In *Coors*, we considered the needs of a brewer who sought to impose customer and territorial restrictions upon its distributors in order to ensure, among other things, that its beer remained refrigerated in storage and distribution from the brewery to the consumer. We pointed out, however, that a supplier of a trademarked product may have available to it means less anticompetitive than territorial or customer restrictions to ensure a reasonable measure of quality control at each level in the chain of distribution. Coors beer was brewed by a unique process and required continuous refrigeration. Thus our order in that case permitted the brewer to establish refrigeration standards not only for its own distributors, but downstream for the distributors' customers. The brewer was permitted to hold distributors responsible for inventory rotation by central warehouse customers and at the retail delivery locations where the beer was received from the central warehouse.

Having considered respondents' quality control objectives, we feel that the underlying rationale of our decision in *Coors* is clearly applicable. While the finished soft drinks need not be distributed

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origin as reliably as territorial restrictions. Further, if respondents employed a container dating which would be read without resort to a code, retailers and consumers would be able to monitor and detect the product's age.

through refrigerated channels, the shelf-life of these products is not indefinite; over time, the process of oxidation can sour the taste of these beverages. (Tr. 698, 978–79).[36] Respondents may, however, establish reasonable [38] quality control standards for distribution and storage, including inventory rotation policies, and may further require that each bottler identify itself on the bottle, bottle cap, or on the can so that respondents may reasonably monitor compliance with its quality standards. Clearly, quality control and intrabrand competition are not incompatible.

Under these circumstances, we are unable to conclude that territorial restrictions are reasonably necessary to ensure the taste uniformity or the purity of these products; quality control, trademark protection considerations do not, in this instance, justify the restraint imposed on the sale of the bottlers' finished soft drink products.

V. INTERBRAND COMPETITION

Buttressed by the judge's finding that the "corridor area" exhibits "intense" interbrand soft drink price competition, respondents argue that their restraints on intrabrand competition are reasonable. The judge concluded that the prices which bottlers charge for Coca-Cola and allied products are determined by their costs and interbrand competition (IDF 106) and that bottlers cannot price Coca-Cola and allied products above the prices of other brands, such as Pepsi-Cola and 7-Up, without losing sales. (IDF 108–09). He also found that the bottlers of Coca-Cola frequently offer price promotions (IDF 127–30) and that a restriction on intrabrand competition is procompetitive because it allows the bottlers to focus on interbrand rivals, thereby increasing interbrand competition.

The record shows that Coca-Cola and the allied products compete with a wide variety of beverages. Evidence was adduced at the trial from which a list was compiled of the brand or trade names of products which, to one degree or another, compete with Coca-Cola; the list of brands is lengthy and will not be repeated here. (*See* RFP 157–80). In summary, it includes the names of hundreds of national, regional, and local flavored carbonated soft drink brands; private label soft drinks, the bulk of which are produced by contract canners for food chains and other types of chain stores; powdered mixes such as Kool Aid, Funny Face, and Wylers; and noncarbonated drinks, including such brands as Hawaiian Punch, Gatorade, and fruit juices and drinks. The Coca-Cola bottlers who testified in this proceeding agreed that all such products compete, at least to some degree, with Coca-Cola in bottles and cans. However, their testimony clearly demonstrates that flavored carbonated soft drinks generally and the brands, such as Pepsi-Cola, distributed by **[39]** other bottlers are the Coca-Cola bottlers' primary competitive rivals. As the record in its entirety amply demonstrates, the suppliers of these products exert the greatest influence on their competitive decisions. (*See* Tr. 1324–25; 1533; 3243). Consequently, we will focus mainly on the products which the bottlers have identified as their most important interbrand competition. Presumably, this is where the "intensity" of interbrand competition would be most evident.

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[36] Estimates of this time span are variously given for bottled products as two to four weeks (Tr. 1116–17), three to eight weeks (Tr. 1240–41), 60 days (Tr. 1632), a few weeks (Tr. 979), a month or so (Tr. 2087), and several weeks for cans, if stored in a cool, dark place. (Tr. 1381). In addition, the shelf-life of canned products depends on whether the cans are made of steel or aluminum. Aluminum cans apparently retain taste quality a little longer than steel cans. (Tr. 1116–17, 1239, 1343–44, 2300).

A. FLAVORED CARBONATED SOFT DRINK BRAND COMPETITION

The judge found that there is intense competition in the sale of flavored carbonated soft drinks "which stems from the fact that there is a large number of brands available to the consumer in local markets." (ID 36). As impressive as the number of brands on respondents' list may be, however, it is, in itself, no measure of the intensity of the competitive interaction among the brands or the bottlers or canners which supply them. Indeed, the judge's consideration of interbrand competition at the finished soft drink production and distribution level glosses over the customary practice of major brand bottlers to carry the brands of several different syrup companies, a practice which they refer to as "piggybacking." Nor does the initial decision reflect any analysis of the anticompetitive interbrand effects of geographic market restraints which admittedly permeate the entire industry.[37] We believe that an accurate assess-

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[37] The judge found that intense interbrand competition was evidenced by data showing a decline in Coca-Cola's food store market share during the period 1950 through 1971. In reaching this conclusion, the judge relied on two series of data stipulated by counsel and offered into evidence by respondents. In IDF 163, the judge found that Coca-Cola brand unit sales declined from 41.2 percent of total domestic flavored carbonated soft drink food store sales in 1950 to 24.4 percent in 1965. Unit sales, however, do not take into account the fact that soft drinks are packaged in containers of different sizes; it reflects only the number of bottles and cans sold, not liquid volume. (RX 2B). The record shows that prior to 1955, bottled Coca-Cola was available in only one size, the 6 1/2-oz. bottle. (RPF 253). In subsequent years, new sizes were introduced ranging from 6 1/2 ounces to 64 ounces. Yet on a unit basis, one 32-oz. bottle is the equivalent of one 6 1/2-oz. bottle, although it contains nearly five times as much beverage. Under these circumstances, the comparison of unit sales data before and after 1955 in IDF 163 is meaningless.

The judge also compared statistical case sales of Coca-Cola between 1960 and 1971 and noted that it declined from 22.3 percent of food store sales to 20.8 percent. (IDF 164). The statistical case represents a conversion of the sale of soft drink cases containing all package sizes to the equivalent of 24 8-oz. containers or 192 fluid ounces. As reflected in the stipulation, the "Coca-Cola" sales trend, on a statistical case basis, is as follows:

1955	20.0%
1960	22.3%
1965	19.5%
1970	21.1%
1971	20.8%

RX 2-Z44

However, the stipulation also shows that both total flavored carbonated soft drink food store sales and Coca-Cola brand food store sales increased rapidly during this period. Food store sales in 1955 exceeded 495 million cases. In the

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ment of the condition of interbrand competition in this industry, that is, its "intensity" or "degree" as reflected in the record, must take these factors into consideration. [40]

1. *Effect of Piggybacking on Interbrand Competition at the Bottling Level*

Piggybacking involves the production and sale by a bottler of soft drink brands trademarked by two or more syrup companies. Each syrup company generally grants the bottler an exclusive territory for its brands. In piggybacking situations involving Coca-Cola bottlers, the territories are not always coextensive [41] in size or dimension with their Coca-Cola territories, but they usually overlap to a substantial degree.[38]

The Coca-Cola Company argues that the brands piggybacked by its bottlers evidence interbrand competition. Some insight into respondents' rationale for concluding that competition is intense among a bottler's piggybacked brands was provided by the President of The Coca-Cola Company. According to Mr. Smith: [42]

> [W]hen a product is put on the [retail] shelf the consumer is often unaware of its source. . .so what I am saying is when the consumer is shopping on a shelf or looking

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same year, Coca-Cola brand sales exceeded 98 million cases. By 1971 food store sales topped 1,573 million cases while Coca-Cola brand sales reached nearly 328 million cases. (RX 2-Z44).

Evidence of the meteoric rise in the volume of soft drinks sold during this period and Coca-Cola's relatively stable portion of this sizable volume, particularly since the early 1960s when diet soft drinks emerged as a strong factor in the market (Stipulation No. 3, CX 1244H-I), contradicts the contention that interbrand competition has significantly eroded Coca-Cola's position in the market.

In addition, we note that food store sales data relied upon by the judge fails to reflect Coca-Cola sales in a large number of non-food store outlets (RPF 221-22, RX 2Z41-42), and thus probably understates the brand's true strength. (*See* Tr. 2324). For this reason, the data cannot provide an accurate indication of either the Coca-Cola Company's soft drink syrup and concentrate sales to bottlers or the bottler's sales of finished, flavored carbonated soft drink sales in any local market. Moreover, even within the limited universe relied upon in the initial decision, the fact is ignored that the Coca-Cola Company's allied product lines, including Tab, Sprite, Fresca and Mr. PiBB, which were introduced in the 1960s, had by 1971 captured about 4 percent more of total food store sales. (RPF 273). Had these brands been included, it is evidence that the share of this universe attributable to the Coca-Cola Company's brands did not decline; rather it increased from about 20 percent in 1955 to about 24.8 percent of food store sales in 1971. Similar distortions are noted in the judge's analysis of the Pepsi-Cola brand's 1971 estimated market share of approximately 19.3 percent. This analysis also ignores "Pepsi" sales in non-food store outlets and PepsiCo's sale of such allied products as Diet Pepsi, Patio flavors, and Mountain Dew.

[38] Piggybacking is used extensively in the soft drink bottling industry. The record shows that in 1971, 438 of the 726 domestic Coca-Cola bottlers also distributed at least one soft drink brand not licensed by respondents. (Tr. 689). As a consequence, important national brand soft drinks, such as Dr. Pepper or 7-Up, are in some territories produced and sold exclusively by the local Coca-Cola bottler. Similarly, Nestea, canned ice tea, is sold under a territorial licensing system by 135 national brand bottlers, including 55-60 bottlers of Pepsi-Cola, 45-50 bottlers of 7-Up, and 30 bottlers of Coca-Cola. (RPF 262-63). In New York City, for example, where Coca-Cola is the leading flavored carbonated soft drink brand with a 14 percent market share in 1973, the Coca-Cola bottler sells several allied products and piggybacks both Welch's Sparkling Grape Soda and Dr. Pepper.

Other examples include the Reading Coca-Cola bottler who piggybacks Pennsylvania Dutch Birch Beer and Bottoms Up Chocolate (Tr. 1888-89); the Jamestown, N.D., Coca-Cola bottler who piggybacks 7-Up, Nesbitts Orange, Dads Root Beer, Squirt, and Sunrise Flavors (Tr. 1957); the Coatesville, Pa., Coca-Cola bottler who piggybacks Dr. Pepper and Pennsylvania Dutch Birch Beer (Tr. 2173); the Herminie, Pa., 7-Up bottler who piggybacks RC Cola; and the Dyersburg, Tn., Pepsi bottler who piggybacks Bubble-Up and Dr. Pepper. (See Tr. 961, 1443-45, 1600-01, 2809-10, 2863, 3005-07, 3063).

through a vending machine to pick a product, any product, (it) is in competition with any other product there in my opinion. (Tr. 781–82).

Were we to concern ourselves only with the image of competition which a lengthy recitation of brand names may project, the consumer's imperfect knowledge about who it is that actually supplies the brands might be superficially persuasive, and the effect of piggybacking might be safely ignored.

To the extent these brands represent the sale of syrups and concentrates by competing syrup companies, we acknowledge that they are a factor in the sale of soft drink ingredients to bottlers. (Tr. Oral Argument July 28, 1976 at 71–73). By contrast, however, in the sale of finished soft drink products to retailers, piggybacking allows a Coca-Cola bottler to control the pricing and marketing strategies for each piggybacked brand. (Tr. 1820–23). Thus he may determine unilaterally the extent to which pricing policies respecting one of these brands will be permitted to "cannibalize" sales of his other brands. (Tr. 2007–08). Consequently, if a competing bottler undercuts Coca-Cola and thereby cuts into Coca-Cola sales, the Coca-Cola bottler's only defense may be a responsive price cut. In contrast, if a Coca-Cola bottler who piggybacks Dr. Pepper finds that his price on a Dr. Pepper promotion is cutting too deeply into his Coca-Cola sales, he may find it in his interest to raise the price of Dr. Pepper rather than lower the price of Coca-Cola. (*See* Tr. 3037–38). Thus, the Coca-Cola bottler in New York City, having assessed the potential strength of Dr. Pepper in New York and having determined that its entry was imminent, became a Dr. Pepper "piggybacker"[39] because: "we would rather compete with ourselves than have somebody else compete with us." (Tr. 2302). [43]

Nor is it surprising that a bottler would prefer to shadowbox with "in-house" brands rather than meet the more rigorous competitive challenge of another bottler. In becoming "self-competitive," the bottlers' objective understandably is to "get more new sales volume from a competitor than from themselves." (Tr. 782, 2008). As a result, a Coca-Cola bottler who piggybacks Dr. Pepper, for example, will employ marketing strategies which are designed to take sales away from the brands of other bottlers without losing Coca-Cola volume in the process. (Tr. 1558, 2691). He may, for example, prevent price interaction among his piggybacked brands by selling each of his brands at the same price (Tr. 1822–23); by packaging one brand in returnable bottles and another brand in cans or nonreturnable bottles, thus minimizing head-on package competition between them; or by adopting other strategies depending upon the particular situation. (*Id.*, Tr. 2392–93; *See also* Tr. 2553). While the record shows that bottlers are not always able, in the short run, to prevent one brand from cannibalizing the volume of another (*See* Tr. 2354–55), it also shows that the basic marketing strategy of brand proliferation is to increase the bottler's total sales in the long run or protect his other brands from erosion. (Tr. 2385–86, 3037–38, 2008, 2302). Notwithstanding respondents' vigorous protestations about the "intense" interbrand competition among a bottler's piggybacked brands, their bottlers understand that being self-competitive is not "the real thing."

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[39] It is a policy of The Coca-Cola Company not to license its allied products to bottlers other than Coca-Cola bottlers. (Tr. 675). Consequently, bottlers have at times elected to piggyback certain brands or flavors of another syrup company, knowing that Coca-Cola allied products would not be introduced as competitive brands in their territory. Thus Mr. PiBB, respondent's Pepper-type drink, was not introduced in New York City because the Coca-Cola bottler there elected instead to distribute Dr. Pepper. (Tr. 2301). Had Dr. Pepper entered New York via another bottler, such as the Pepsi bottler, the New York Coca-Cola bottler could have responded by introducing Mr. PiBB. Pursuant to The Coca-Cola Company's policy, however, the New York Coca-Cola bottler not only acquired control of the Dr. Pepper brand, it knew that no other bottler would have access to the competing Pepper-type drink, Mr. PiBB. Similarly, Coca-Cola bottlers who handle their own flavor lines understand that competing Fanta flavors will not be introduced in their territories by any other bottler. (*See* Tr. 1600–01, 1094–95, 1226, 1666).

Furthermore, evidence of the potential effect of piggybacking on the structure of the flavored carbonated soft drink bottling industry indicates that the practice tends to increase concentration. For example, in the territory of the San Antonio, Texas, Coca-Cola bottler, a large number of brands are available to the public. The bottler, when asked about interbrand competition, identified Pepsi-Cola, Diet Pepsi, and the allied products of PepsiCo.; Royal Crown and its allied products; Dr. Pepper, Diet Dr. Pepper, Canada Dry and its allied products; 7-Up; Shasta, Barqs; Nestea; Big Red; Orange Crush and its line of flavors called Matthews Dot; numerous flavor lines offered by other bottlers; and private label house brands of the major chains, such as Handy-Andy, among others. [44]

The record also shows, however, that in San Antonio, Pepsi-Cola and its allied products and 7-Up and its allied products are manufactured and distributed by the same bottler who, in addition, offers his own line of flavors. (Tr. 2501). Another bottler manufactures and distributes RC Cola, Diet Rite Cola, and the Nehi Flavor line. (Tr. 2501–02). The Canada Dry bottler, in addition to Canada Dry and its line of ginger ale, sodas, and tonics, also manufactured and distributes Frosty Root Beer, Orange Crush, and the Matthews Dot flavors. (Tr. 2502). Big Red, which respondents cite as a strong regional competitor, is manufactured and distributed by the same bottler who manufactures and distributes Barqs flavors. (Tr. 2503–04).[40] [45] Evidence of this high level of concentration among the suppliers of the various piggybacked products strongly suggests that the "intensity" of interbrand competition cannot be realistically assessed simply by naming and counting brands available in a market. Indeed, we find much more significant the fact that piggybacking tends to increase the concentration of brands controlled by the strongest bottlers in a territory, while territorial restrictions shield them from the competition of extra-territorial interbrand bottlers.

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[40] Of all the flavored carbonated soft drink brands available in the food stores in San Antonio, Coca-Cola is the market leader. (RX2–Z37). The Coca-Cola bottler testified that his share of the flavored carbonated soft drink market sold through food stores in San Antonio varied anywhere from a low 34 percent to a high of about 40 percent (Tr. 2485–86, 2532–33) over a period of several years. (Tr. 2533–34). He further estimated that the Pepsi-Cola share varied from 17 percent to about 21 percent; Dr. Pepper from 8–11 percent; RC Cola from 6–8 percent; and Big Red, the strong regional brand, from 9–10 percent of the market.

Consequently, if the combined market of the San Antonio Coca-Cola bottler and the Pepsi-Cola bottler had fallen

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B. TERRITORIAL RESTRICTIONS LESSEN INTERBRAND COMPETITION AMONG SOFT DRINK SUPPLIERS

The judge also ignored evidence showing that territorial restrictions which prevent intrabrand competition also tend to lessen interbrand competition. (Tr. 960–61, 1879, 1900–1900A). Because the universe of potential customers available to a bottler is strictly limited by the boundaries of his territory[41] [46] he is prevented from competing against Pepsi-Cola bottlers and other soft drink suppliers interbrand for the business of retailers located within another Coca-Cola bottler's territory. (Tr. 887–88). Consequently, the restriction eliminates important potential interbrand price competition between a Coca-Cola

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to their low points at the same time, these two bottlers still controlled 51 percent of the flavored carbonated soft drinks sold through food stores in San Antonio; and this would not reflect their sales through non-food store outlets. In fact, the Coca-Cola bottler alone placed about 8,000 vending machines throughout his territory. (Tr. 2481). Furthermore, according to the testimony of this defense witness, the four leading soft drink bottlers in his territory controlled about 68 percent of the total food store flavored carbonated soft drink sales, including the private label products sold by the chain stores. (Tr. 2533). Despite brand availability at the retail level, the evidence indicates that the San Antonio local bottling industry may be advancing toward fairly tight oligopoly.

Similarly, the record shows that in the Albany, N.Y., territory, Pepsi-Cola, according to the bottler called as witness by respondents, is the leading brand with a flavored carbonated soft drink brand market share of about 21–22 percent; Coca-Cola has about 16–17 percent. (Tr. 2935). Thus, these two brands alone account for about 37 percent of food store sales in Albany. In addition, however, the Pepsi-Cola bottler also controls Hires Root Beer; Orange Crush; Schwepp's carbonated soft drink line; canned Lipton Tea; and PepsiCo's allied products, including Mountain Dew. (Tr. 2863).

[41] In overruling *Schwinn*, the court in *GTE* made it clear that the degree of intrabrand competition foreclosed by a vertical restriction provided no basis for distinguishing situations in which the *Schwinn* per se rule would or would not be applied. *GTE, supra*, at 71,896. Under *GTE*, however, territorial restrictions must be evaluated by the traditional rule of reason framework of analysis to determine if they produce a demonstrable effect on competition. Thus the degree of foreclosure is a factor in assessing the overall competitive effect of the restraint. (*See generally Elfman Motors, Inc.* v. *Chrysler Corp.*, 1977–2 Trade Cases, ¶61,650 at 72,683 567 F.2d 1252).

The Coca-Cola Company's territorial restriction is a demonstrably more severe restraint on intrabrand competition than the dealer location clause imposed by *GTE*. GTE designates the location of its retailer dealer's outlet, but apparently does not limit the area from which a retailer may draw its customers. The territorial restrictions involved here not only limit the area from which bottlers may solicit customers, they eliminate the retailer's option to do business with the Coca-Cola supplier offering the most competitive deals. Furthermore, as the restrictions are applied by respondents, they limit retailers in reselling the Coca-Cola and allied products; usually the product purchased from a bottler may be resold by a retailer only at outlets located within the territory of the bottler from which it was purchased. Thus, the vertical restraint in GTE's franchise does not constitute an exclusive territory (*GTE* at 71,898); nor does it ensure GTE's retailers freedom from intrabrand competition. Unlike the situation in *GTE* and *Snap-On-Tools Corp.* v. *F.T.C.*, 321 F.2d 825 (7th Cir. 1963), in which customers were free to buy in any territory from any dealer, thus leaving open the potential for intrabrand competition among the dealers, respondents' practice mandates exclusive territories and completely eliminates intrabrand competition among the bottlers of Coca-Cola and allied products.

bottler confined to a territory and virtually all interbrand suppliers serving customers in areas adjacent to his territories.[42] [47]

Territorial Restrictions Industrywide Lessen Interbrand Competition

When this effect is considered in light of the fact that respondents' territorial restrictions are nationwide in scope, and in light of the further fact that territorial restrictions are an industrywide practice restricting "Pepsi" bottlers and the bottlers of numerous other major and secondary brands throughout the country (RPF 17), it is difficult to avoid concluding that territorial restrictions, vertically imposed, have seriously impaired interbrand competition. Not only are Pepsi-Cola bottlers and other soft drink suppliers shielded by respondents' restriction from the competition of all but one Coca-Cola bottler for the business of virtually any given retail outlet, the industrywide nature of the restraint insulates Coca-Cola bottlers from unimpeded competition of potential interbrand bottlers.

Evidence of this insulating effect is reflected in the pricing behavior of respondents' bottlers in territorial overlap situations. Overlaps occur when, for example, the territory of a Coca-Cola bottler encompasses all or a part of the territories of two or more bottlers of a competing brand, such as "Pepsi." Like the Coca-Cola bottlers, "Pepsi" bottlers are also confined by territorial restrictions which prevent them from competing with each other. In these situations, the Coca-Cola bottler will, in any given segment of this territory, compete with only one of the Pepsi bottlers. For example, the record shows that Warrenton, Virginia, is outside the territory of the Washington, D.C., Pepsi bottler, but within the territory of the Washington Coke bottler. Because the Warrenton Pepsi-Cola bottler has at times charged lower prices than the large Pepsi bottler in the metropolitan Washington area, the Coca-Cola bottler has been forced to respond with lower prices in that part of its territory. As Mr. Wilbert N. Sales, Vice President and General Manager of Washington Coca-Cola Bottling Co., Inc., testified:

> A. . . . Warrenton is priced well below Alexandria, and the reason for that is competition.
>
> Q. Could you explain what you mean by that?
>
> A. Well, basically in that market it is Pepsi-Cola. Pepsi-Cola out of Charlottesville,

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[42] This is illustrated by pricing data relied upon by respondents. The record shows, for example, that cases of 24 12-ounce cans of both Coca-Cola and Pepsi-Cola have been offered at wholesale for $3 in Baltimore. At the same time, a case of Coca-Cola in 12-ounce cans was offered to retailers for $2.90 by a different bottler serving Havre de Grace, Maryland. Yet the Coca-Cola bottler who served Havre de Grace through a distribution center was prevented by the territorial restriction from offering or selling canned or bottled Coca-Cola to retailers in the Baltimore territory, thirty miles away (Tr. 2960), in competition with the Baltimore Coca-Cola bottler, intrabrand, and the Baltimore Pepsi bottler, interbrand. (*See* RPF 192, Tr. 1564).

Va. They are priced way down. . . . This is the way he operates, and he couldn't care less whether he makes money or not, so there is the problem. (Tr. 1259).

[48] In respondents' view, the fact that the Washington Coca-Cola bottler charges lower prices in overlap areas to meet competition from Pepsi bottlers, other than its major Pepsi bottler competitor in the Washington, D.C., metropolitan area, is evidence of interbrand price competition rather than the lack of it. (Ans. Br. 88). This is correct to the extent that interbrand competition exists in both instances, but it can also be reasonably inferred from this evidence that interbrand competition between Coca-Cola and Pepsi-Cola may be significantly less "intense" in the Washington metropolitan area than it is in the Warrenton area. Moreover, the Pepsi bottler serving Warrenton is, as a result of the territorial restrictions imposed by PepsiCo, precluded from expanding into Northern Virginia and perhaps Washington whenever higher "Coke" or "Pepsi" prices prevail in these areas.[43] Consequently, retailers and consumers in a major metropolitan market are deprived of the benefits of an open market in which the Washington Coke bottler probably would have had to meet the interbrand competition of the Warrenton Pepsi supplier in a wider geographic area and, at the very least, would have had to consider this bottler a serious potential interbrand price competitor outside of the Warrenton area, a consideration which Washington metropolitan bottlers may completely disregard. (Tr. 1314).

What has occurred between the Warrenton Pepsi bottler and the Washington Coca-Cola bottler is not simply an isolated episode without broader competitive significance. The situation in Warrenton illustrates a fundamental limitation on interbrand price competition in the soft drink bottling industry not only in overlap situations, but as a direct result of territorial restrictions nationwide. Recognizing this, respondents contend that disparities in the wholesale list prices of bottlers in different territories have no probative value because bottlers use alternative pricing strategies; some bottlers offer lower list prices, other bottlers adopt higher list prices but engage in more frequent promotions. (Ans. Br. 75, 88).[44] [49]

The fact that different bottlers use different pricing strategies and price levels at wholesale and during promotions in different territories is, itself, a strong argument for lifting the restriction in order to allow the various prices and pricing strategies to clash head-on in the marketplace. We regard the uncertainties created by the confrontation of pricing strategies as the very essence of competition which the present system of territorial restrictions, to a large extent, eliminates. Whether a Coca-Cola bottler's pricing strategy is to compete on the basis of wholesale list prices or price promotions, or both, the fact remains that territorial restrictions rule him out as an actual or potential competitive rival of all soft drink suppliers, intrabrand and interbrand, in every locale beyond the territory assigned to him by respondents. In view of the fact that respondents' bottlers and virtually all other major brand bottlers are similarly restricted, we conclude that the practice is, to a substantial degree, adversely affecting interbrand competition at the bottling level of this industry.[45] [50]

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[43] Conversely, the restriction would allow the Charlottesville Pepsi Bottler to raise his prices in the portions of his territory located outside of the Warrenton area without regard for a lower price which the Washington Coca-Cola bottler may be charging at the time. (Tr. 1259–60).

[44] Obviously, a wholesale price considered "low" by one bottler may be considered high by another bottler. Similarly, what one bottler considers "frequent" promotions may be considered occasional by another, just as a "deep" price promotion in one territory may be considered miserly in another.

Thus we find reflected in the testimony of virtually every bottler who testified at the hearing and the top management of The Coca-Cola Company the fear that intrabrand competition would, in fact, cause prices to fall. The President of The Coca-Cola Company testified that absent territorial restrictions, there would be price competition at the wholesale level which does not exist under the territorial system. (Tr. 739).[46] In the opinion of another experienced executive of The Coca-Cola Company:

> I think under this "walls down" thing. . . . No territorial exclusivity, no territorial restrictions, that Coca-Cola and our other products, or products from other bottlers would find its way into chain stores warehouses.
>
> I think . . . that pricing would be more active than it ever had been. [I] think that it

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[45] Respondents contend that territorial restrictions promote competition at the syrup-producing level because they make possible a means for the lesser-known brands of their syrup company competitors to enter easily into new local markets. (Ans. Br. at 91, IDF 159–162, RPF 262–64). As we have previously noted, Coca-Cola bottlers and other major brand bottlers piggyback the "lesser" brands of other syrup producers within exclusive territories granted to them by those producers. To this extent both piggybacking and exclusive territories may assist the company's entry into the soft drink syrup production industry. However, we are not here dealing with the reasonableness of territorial exclusivity conferred by a small syrup producer of one of the "lesser" brands.

Respondents argue further that removal of territorial restrictions on the sale of Coca-Cola and the allied products will generate competitive forces which will result in the demise of many Coca-Cola bottlers and the secondary brands which they piggyback into local markets. (Respondents' "small bottler" arguments are considered, in detail, *infra).* While the record shows that the number of independent Coca-Cola bottlers has, notwithstanding respondents' territorial restrictions, declined significantly since 1968, the record does not indicate the fate, in local markets, of the secondary brands formerly piggybacked by bottlers who have sold their businesses to neighboring bottlers or have consolidated their territories or bottling plants. (*See* Text at 66, fn. 63 *infra).* Presumably the secondary brand syrup producers were free to franchise either the bottler which took up the distribution of Coca-Cola within the territory from which its predecessor withdrew or any other independent bottler distributing other brands in the local territory or neighboring territories. (See Tr. 1672, 1684, 1668). Thus The Coca-Cola Company argued in *Sulmeyer* v. *Coca-Cola, supra*, in defense of a complaint alleging that it was monopolizing the business of the independent Coca-Cola bottlers which it secured for the distribution of its lemon-lime flavored product, Sprite, that the universe of independent bottlers capable of effectively bottling and distributing the lesser-known brands was not limited to those bottlers who market Coca-Cola. After reviewing the evidence adduced at the trial, the Fifth Circuit Court of Appeals agreed with respondents, noting that a secondary brand "could reach the consumers in a given area through a franchise agreement with any independent bottler." (at 850). We are, therefore, unable to accept respondents' contention that the territorial restrictions which they impose on the sale of Coca-Cola and allied products are necessary to ensure the competitive viability of syrup companies which compete with respondents.

[46] *See* IDF 171.

> would mean that . . . to be competitive, and to get the business, we would have to make up our minds either we want the business or don't want it. We would be forced to reduce our prices to the principal customers. (Tr. 992–93).

This assessment, by key management personnel of The Coca-Cola Company, was echoed by bottlers who predicted wholesale price reductions if the restrictions were lifted. (Tr. 1568, 2459, 2855). Yet it would not, as the record shows, just be the price of Coca-Cola which would be more active as a result of intrabrand competition; the suppliers of hundreds of other interbrand soft drink products must be responsive to the prices of Coca-Cola and the allied products and they could not afford to ignore for too long any reductions in the wholesale price of these products. [51]

2. *Intrabrand Competition in the Sale of Coca-Cola and the Allied Products Would be Likely to Result in Increased Competition in the Sale of Soft Drink Beverages*

Respondents argue that Coca-Cola and the allied products are sensitive to the prices of competing brands, and as a result, the bottlers' pricing decisions must be influenced by the interbrand competition in their respective territories. As respondents submit, there is evidence of price sensitivity in the record; however, as we have determined, the "intensity" of interbrand competition in the soft drink bottling industry is affected by piggybacking and substantially diminished by the territorial restrictions imposed by respondents and similar restraints imposed industrywide by other syrup companies. As a result, interbrand competition may not be fully exploiting the price sensitivity of respondents' soft drinks, and equally important, as a consequence of the restraints on intrabrand competition here challenged, Coca-Cola and the allied products are not fully challenging the sensitivity of other soft drink products to their prices.

Evidence adduced at the trial by respondents shows that Coca-Cola and the allied products compete with such products as local, regional, and national brand flavored carbonated beverages; private label soft drinks; and to some extent, powdered mixes and noncarbonated drinks. (RPF 157–80). To the extent Coca-Cola competes with and is price sensitive to these types of products, it may be concluded, particularly in view of the fact that Coca-Cola is the nation's leading flavored carbonated soft drink premium brand and a dominant brand in many local markets across the country, that other soft drink products are equally, if not more, sensitive to Coke prices. According to the bottlers of other brands, price competition of Coca-Cola takes sales away from Pepsi-Cola (Tr. 2886–87, 2889–90), 7-Up (Tr. 2682), Nestea (Tr. 3456), and Lipton canned ice tea (Tr. 3562–63). (RPF 219). Mr. Hurst, the marketing manager for Nestea Co., testified that his canned ice tea product loses sales if it is one cent higher per six-pack than the premium priced carbonated soft drinks such as Coca-Cola. (Tr. 3456-57). Similarly, in response to questions propounded by respondents' counsel, the defense witness, who bottles Pepsi-Cola, Dr. Pepper, and Bubble-Up in Dyersburg, Tennessee, testified:

> Q. Can you afford to sell Dr. Pepper at a higher price than Coca-Cola is being sold in your territory?
>
> A. Oh, definitely not.
>
> Q. Now, are we talking about a dollar more, or a few cents per case? [52]
>
> A. I don't think—well, we would not let ourselves be caught in a situation whereby, over an extended period of time, any major product was being sold at a cheaper price than our products.
>
> Q. You mean when you say cheaper. . . .
>
> A. Not even one or two or three cents a bottle or carton. (Tr. 3046).

While respondents, in their answer brief, attempt to minimize the importance of intrabrand competition among the bottlers of Coca-Cola, the acknowledged sensitivity of interbrand soft drink products to the price of Coca-Cola and the allied products refutes respondents' contentions. Because Coca-Cola is, as respondents' evidence solidly confirms, an important interbrand competitive force in the market, a practice which eliminates intrabrand price competition has adverse repercussions throughout the entire soft drink industry. As the evidence clearly demonstrates, lower prices for Coca-Cola would, in turn, exert enormous downward pressure on the price of interbrand flavored carbonated beverages and, to a lesser degree, on Kool Aid, Funny Face, fruit juices, and all other soft drink products which, according to the bottlers, compete with Coca-Cola.

For this reason, the judge's conclusion that competition among the independent bottlers of a premium brand soft drink such as Coca-Cola would "dilute" their competitive efforts against interbrand bottlers could not, consistent with the pricing dynamics of this industry, apply to pricing behavior. Rather than dilute the Coca-Cola bottlers' competitive impact interbrand, the record shows that intrabrand price competition would, perforce, strengthen their impact considerably. Thus it does not appear that price competition in this industry is enhanced by respondents' territorial monopolies. In fact, evidence in the record demonstrates that exactly the opposite is true. We conclude that respondents' territorial restrictions substantially lessen competition among soft drink suppliers in the "corridor area" and the rest of the country, in violation of Section 5 of the Federal Trade Commission Act.[47] [53]

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[47] Respondents and intervenors contend that the legality of their territorial licenses was judicially upheld in 1920

(Continued)

VI. Relief

A. RETURNABLE, REFILLABLE PACKAGING

Respondents' bottlers package their products in two basic types of containers: those which the consumers usually discard after use and those which may be returned to the bottler, purified, and reused. Both types of containers offer consumers distinct advantages. Nonrefillable cans and bottles, or nonreturnables as they have been referred to in this proceeding appeal to consumers who prefer convenience, throw-away packaging and are willing to pay for it. Refillable bottles, in contrast, appeal to consumers who are concerned more with economy than [54] convenience.[48] For reasons stated below, we find it unnecessary to disturb established bottling territorial relationships which now exist with respect to the sale of Coca-Cola and allied products in returnable, refillable bottles. As in litigation involving mergers which violate Section 7 of the Clayton Act in which partial rather than full divestiture provides satisfactory relief, *Federal Trade Commission* v. *PepsiCo, Inc.*, 477 F.2d 24, 29–30 (2d Cir. 1973); *U.S.* v. *Reed Roller Bit Co.*, 274 F. Supp. 573 (W.D. Okla. 1967); *Warner-*

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in The *Coca-Cola Bottling Co.* v. *The Coca-Cola Co., supra*. In ruling on the legality of the territorial licenses in response to the actions The Coca-Cola Company had taken to put its bottlers out of business, however, the district court was not required to decide, nor did it have before it, the legality of the territorial restrictions which are now before us. The basic question before the court there was whether The Coca-Cola Company had the right arbitrarily to terminate the bottlers over disputes concerning the price of syrup. The consent decree eventually entered in that case reflected, in part, the court's ruling that the bottlers have a right to purchase Coca-Cola syrup and to use the trademark, in perpetuity, and to be free, not from the threat of competition among themselves, but from arbitrary termination by The Coca-Cola Company. The regulation of competition among the independent bottlers was not an issue joined before the court; the provisions of the consent decree respondents rely upon in support of the restrictions here challenged apparently were inserted by the parties to accommodate their private interests.

More directly on point is the decision of the district court in *Tomac, Inc.* v. *Coca-Cola Co.*, 1976–2 Trade Cases, ¶60,988, in which the court, in a private treble damage action, overturned a jury verdict finding respondents' territorial restrictions illegal. The judge in *Tomac* concluded that the restraint was reasonable because it promoted a legitimate business purpose by providing incentives for capital investment and enhancing competition. (at 69,381). For reasons discussed at length in this opinion, we respectfully reach a contrary conclusion. We feel it is, in these circumstances, appropriate also to note that decisions of federal and state courts approving a practice challenged by the Commission would not foreclose a contrary FTC Section 5 decision, nor would consent decrees entered by agreement of the parties in settlement of a private suit. *FTC* v. *Sperry & Hutchinson*, 405 U.S. 233, 239 fn. 4 (1972).

[48] As we mentioned earlier, prior to 1955, the only unit in which bottled Coca-Cola was offered was the 6 1/2-ounce returnable container. (Unless otherwise indicated, the term "returnable bottle" or "returnables" refers to the type of bottle which can be refilled and reused by the bottler.) The popularity of returnables declined after disposable containers were introduced, then increased and stabilized. This recent stabilization is attributed principally to adjustments in the deposit structure and the fact that economy-minded purchasers are buying refillable bottles and returning them while convenience buyers are purchasing nonrefillable packages. (RPF 349).

Today the refillables are an important competitive factor in the market, accounting for about 55 percent of the sales of Coca-Cola in bottles and cans on a volume basis. (RPF 348, Tr. 3633).

From territory to territory, the percentage of soft drinks sold in refillable bottles varies. (Tr. 3758–59, 3777–78; RX 7). For example, 30 percent of the sales of Coca-Cola in bottles and cans in Washington, D.C., are packaged in refillable bottles (Tr. 1167); 65 percent in Hartwell, Georgia (Tr. 1384); 70 percent in Spirit Lake, Iowa (Tr. 1462) and the State of Iowa generally (Tr. 1463); 30 percent in Wilmington, Delaware (Tr. 1541–42); 25 percent in Havre de Grace, Maryland (Tr. 1542); 75 percent in Charleston, West Virginia (Tr. 1542); 54 percent in Miami (Tr. 1542); 74 percent in Montross, Virginia (Tr. 1633); 40 percent in Reading, Pennsylvania (Tr. 1916); 20 percent in Coatesville, Pennsylvania (Tr. 2172); 51 percent in San Antonio (Tr. 2487); 45 percent in Stockton, California (Tr. 2567); 55–57 percent in Palo Alto, Burlingame, and San Mateo, California (Tr. 2610); 60 percent in Jamestown, North Dakota (Tr. 1982); and 70 percent in Ada, Oklahoma (Tr. 2670). (*See also*, Text at 17 *supra).*

Lambert Co., 87 F.T.C. 889–90, 88 F.T.C. 503 (1976); *RSR Corp.*, 88 F.T.C. 873, 892–97, we have here determined that partial relief, which is limited to lifting the restrictions as they apply to nonrefillable containers, is fully adequate in the interest in maximizing both intrabrand and interbrand competition. [55]

We have carefully considered complaint counsel's suggested option of placing an identification mark on each bottler as a method of preserving the competitive viability of the refillable bottle, but we are unable, on the basis of the record evidence, to agree with their contention that less restrictive measures are viable alternatives in the context of a system in which refillable bottles are purchased and used by numerous independent producers of a nationally trademarked finished soft drink which is also offered in nonrefillable bottles and cans.

1. *Economy of Returnable Bottles*

It is uncontroverted in the record that in virtually every territory in which refillable and nonreusable packages are offered, Coca-Cola is, on the per-ounce basis, significantly cheaper in the refillables,[49] and the advantage is evident notwithstanding the fact that these bottles initially cost the bottler more than cans and disposable bottles, and the further fact that retailers generally take a larger markup on returnable bottles to compensate for the additional cost of handling the empties returned by consumers. (RPF 132). [56]

The price disparities reflected in this record are, to a large extent, explained by the fact that when a consumer buys soft drinks in nonreturnable bottles and cans, the bottler, at wholesale, and the retailer must recover the full cost of each beverage container with each sale.[50] In contrast, the full cost of a refillable bottle ordinarily need not

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[49] Evidence of the economy of the returnable bottle is reflected in the per-ounce price differentials between Coca-Cola in returnable bottles and nonreturnable containers. For example, in July, 1971, it cost the consumer in Baltimore approximately 33 percent more per ounce to buy Coca-Cola in 16-ounce nonreturnable bottles than in 16-ounce returnable bottles, and 66 percent more per ounce in 12-ounce cans than in 16-ounce returnable bottles. (Tr. 982). In Wilmington, Delaware, the retail price of 32-ounce returnable bottles of Coca-Cola is four for $1.69 or 1.32 cents per ounce; the prevailing retail price for cans is six for $1.49 or 2.06 cents per ounce, 36 percent more expensive to the consumer on a per-ounce basis. (Tr. 1541). In Montross, Virginia, the 16-ounce returnable bottle retails in supermarkets at 1.08 cents per ounce (Tr. 1680); cans retail at 2 cents per ounce or approximately twice as much. (Tr. 1680, 1692). In Jamestown, North Dakota, the current retail price per ounce of Coca-Cola in 32-ounce returnable bottles is 1.2 cents; the price per ounce in 32-ounce nonreturnables is 1.5 cents and in cans, 2.2 cents. (Tr. 1981). Coca-Cola in 16-ounce returnable bottles is, on a per-ounce basis, 29 percent cheaper than Coca-Cola in 16-ounce nonreturnables; 27 percent cheaper than Coca-Cola in 32-ounce nonreturnables; 16 percent cheaper than Coca-Cola in 64-ounce nonreturnables; and 61 percent cheaper than Coca-Cola in 12-ounce cans in Reading, Pennsylvania. (Tr. 1925). In San Antonio, Texas, the prevailing retail price per ounce for Coca-Cola in 16-ounce and 32-ounce returnable bottles is about a penny. Coca-Cola in 48-and 64-ounce nonreturnable bottles retails at about 1.5 cents per ounce, or 50 percent more expensive, and Coca-Cola in cans retails at 1.9 cents per ounce, or 90 percent more expensive. (Tr. 2488, 2551; RPF 208).

[50] The record shows that a case of 24 12-ounce aluminum or steel cans costs about $1.44 or 6 cents per can. The Coca-Cola bottler in Spirit Lake, Iowa, for example, testified that Coca-Cola in his territory in 16- and 32-ounce returnable bottles is about 50 percent cheaper than Coca-Cola in cans, even though a case of 24 empty 12-ounce cans

(Continued)

be recouped all at once, but can be spread over the number of trips the bottler can expect the bottle to make before it is lost, destroyed, or no longer usable. (Tr. 997).[51] Consequently, if a 16-ounce returnable bottle which costs 12 cents survives 18–20 trips, it generates a container cost of only a fraction of a cent per trip. (Tr. 1461–62, 2488, 3996). As one bottler testified:

> when I price my packages I add right on top, the cost of the package. A 10-ounce package, for instance, of a returnable Coke is $2.50 a case . . . 240 ounces, so we are talking about 1.1 something (cents per ounce).
>
> When we talk about a 10-ounce NR (nonreturnable) package, we are talking about $3.60 a case for 240 ounces, probably 1.5 (cents) per ounce, so that is the price of convenience. (Tr. 2149, RPF 209). [57]

2. *Bottle Trippage*

The record shows that in pricing his packages, a bottler must be able to anticipate, with a reasonable degree of accuracy, his returnable bottle requirements and glass "float" inventories.[52] (Tr. 700, 735, 2486; RPF 131). While bottlers continuously invest in returnable bottles to replace those which are lost or no longer usable (RPF 69), the territorial restrictions permit the bottler to anticipate that most of the reusable bottles he puts into the market will be returned by the consumers to the stores within his territory and will be returned by those stores to him. As a result, a trippage rate, which represents the average number of cycles or reuses a bottler can expect from a bottle, can be determined in each territory (Tr. 3635)[53], and used by the bottler in allocating container costs in accordance with his anticipated trippage experience. Generally, the lower the trippage rate in a

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costs him $1.44 while a case of 12 empty 32-ounce returnable bottles costs him about $3.11. Yet because his trippage rate is about 25 per bottle, his container cost per case for 32-ounce returnables (*i.e.*, 384 ounces) is about 11 cents per trip, in contrast with the full $1.44 per case (*i.e.*, 288 ounces) on one-way bottles or cans. (Tr. 1462).

[51] The nonrefillable bottle is not designed to withstand the punishment of reuse. Made of thinner glass than the refillables, products liability considerations dictate that it be used only as a one-way, one-fill container. (Tr. 3765–68). While some jurisdictions have enacted litter laws which require the consumer to pay a deposit, which is refundable upon the return of nonrefillable bottles and cans, the containers reclaimed are not returned to the bottler for reuse. Instead, the nonrefillable bottles recovered from post-consumer waste streams are processed or recycled into crushed glass or cullet for glassmaking processes. Unlike the refillables, then, the bottler cannot spread the cost of a returnable, nonrefillable bottle or can over more than one sale.

[52] The term "float" refers to the total number of refillable bottles of a given type in the bottler's system; it includes those in the inventories of both the bottler and the retailers in his territory as well as those in the homes of consumers. (Tr. 3769). A bottler's minimum "float size" equals his sales multiplied by his anticipated turn-around period. Thus, if the bottler's turn-around time is six weeks and on the average he sells 100 24-bottle cases of returnables per day, five days a week, his float size would be approximately 3000 cases or 72,000 bottles [100 (cases) X 24 (bottles per case) X 5 (days) X 6 (weeks turn-around time).]. (Tr. 3770).

[53] The trippage rate, in turn, depends upon a bottler's "float" size and estimated turn-around time (or the anticipated time it takes each bottler on an average to recover an empty from the consumers in his territory) and the bottler's loss rate. Thus, in a territory in which sales remain constant, "float" size is constant, and turn-around time is constant, the replacement rate would be equivalent to the loss rate, and the bottler would purchase just enough bottles to replace those which have been lost or destroyed. In contrast, in territories in which sales are increasing, the bottler must not only replenish the bottles he has lost, but also invest in a bigger "float;" if sales are decreasing, on the other hand, the bottler's "float" itself may supply his bottle needs so no new investments in glass may be required. (Tr. 3636).

territory, the more rapidly the bottler must recoup the bottle's full cost, thus increasing the per-ounce price of the soft drink.[54] [58]

3. *Bottle Recapture*

In assessing the impact of the order proposed by complaint counsel, it is pertinent in the context of respondents' bottler network that the use of refillable bottles makes economic and competitive sense only if each bottler is able steadily to recapture from the market an adequate, predictable supply of used bottles to service his production requirements. Consequently, there are two major impediments to intrabrand competition in the use of refillables: First, retailers will, from time to time, switch their Coca-Cola bottler supplier; and second, consumers will buy and return bottles to different retailers. Over an indefinite time, then, the refillable bottles provided by a number of bottlers will periodically be returned by consumers either to the store from which they were originally purchased or to a different store supplied by the same or different bottlers. As a result, bottle recapture, under these circumstances, would be unpredictable and economically burdensome. (Tr. 2996–98, 2027). Even if the bottler were to place an identification mark on his bottle, it would be impractical and costly to expect the retailer to notify each bottler whose bottles he may have collected or to require the bottler to divert his trucks to pick up a few empty bottles from retailers who, at the time, may be purchasing "Coca-Cola" from a competing bottler. (Tr. 2544–49).

Nor would the burden of recapture be substantially reduced if a bottler picked up all of the empties, regardless of their source, from each of his customers. Each bottler individually purchases his returnable bottle float and must be able to anticipate his bottle needs based on trippage experience in his territory. Retail outlets which collect large numbers of returnable bottles would provide an abundance of bottles to their suppliers, while other bottlers serving retailers which collect relatively few bottles may experience shortages. Because a bottler would be unable to predict the retail customers he may acquire or lose over time, or their locations, and because bottlers maintain glass inventories of varying sizes, there can be no assurance that the number of bottles a bottler puts on the market will, on a random basis, equal or even closely approximate the number he may pick up in return. It would be virtually impossible for a bottler to determine, with a reasonable degree of accuracy, what portion of his float outstanding in the market will be returned to him for reuse. [59]

Alternatively, if each bottle carried an identification mark and all bottlers picked up all empties from their respective customers, each bottler would be picking up other bottlers' bottles, backhauling the empties, storing them, and notifying the other bottlers who would have to pick them up from widely dispersed collecting bottlers, thus substantially increasing the handling costs associated with the use of returnables while diminishing their economy advantage. It has been stipulated on this record that the use of returnable bottles is incompatible with central warehouse distribution by retailers largely due to the impracticality and costs of having the retailer collect, backhaul, sort, and store empty bottles for the bottlers. Nothing in this record suggests that it would be any more practical or much less costly for a bottler to perform a central warehouse function for the return of other bottlers' empty bottles.

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[54] **In territories in which returnable bottles are offered, the record shows that trippage rates vary from as low as five in some territories to as high as 30 in others. (Tr. 2579, 2995, 1859; RPF 344).**

Similarly, a credit system which would permit a bottler to use bottles purchased by competitors would probably not result in a competitively viable distribution of empties in accordance with the bottlers' bottle needs or investments. Bottlers may offer a wide range of refillable options, including 6 1/2-ounce, 10-ounce, 16-ounce, 26-ounce, and 32-ounce sizes with different investments in each size; and while some bottlers offer most sizes, other bottlers offer only one or two. Consequently, a bottler who maintains a sizeable float which presently services his production runs may end up, from week to week, with too few bottles actually on hand against which credits could be claimed to compete effectively for returnable bottle sales. This could occur, for example, either because a bottler may, as we mentioned, lose retail accounts which collect large numbers of empties or because he may be collecting an assortment of bottle sizes, some of which may not be compatible with his bottling line equipment, or because he has collected too few bottles in each size to offer any size on a competitive basis.[55]

While an increase in the amount of the deposit a bottler may require might protect his investment in glass bottles (Tr. 2097, 3098–3100), the competitive potential of the returnable bottle system would likely be lessened since higher deposits would probably meet with appreciable consumer resistance and encourage a shift to disposables. (Tr. 3051, 2522, 996, 2871, 1994). Nor would intrabrand competition be [60] fostered if bottlers had to invest continuously in new bottles or even used bottles, assuming a secondary used bottle market were to spring into existence, to compensate for wild, frequent fluctuations in float. (Tr. 998).

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[55] Even if several bottlers were to form a cooperative for the production of soft drinks in refillable bottles, the recapture problem would still exist vis-a-vis the members and nonmembers of the co-op. (*See* Tr. 2139–41).

Under these circumstances, we find it unnecessary to lift restrictions on the sale of Coca-Cola and allied products in refillable bottles.

Rather, as the record shows, fully adequate relief in this matter necessitates only the lifting of the restriction as it affects the sale of these products in the nonrefillable containers. Because the relative market strength of convenience and returnable refillable packaging is largely dictated by a price spread sufficient to maintain the consumers' participation in the return system, any downward price movement resulting from intrabrand competition in the sale of nonrefillables would directly influence the price of refillables. Conversely, a viable refillable bottle system operating in the context of an exclusive territory will provide each bottler with a potent price-competitive package. The relief entered in this proceeding will, therefore, differentiate between reusable and nonreuseable bottles and cans based upon demonstrated economic effect. (*GTE, supra).*

4. *Split Delivery*

We are mindful of respondents' defensive arguments that the use of refillable bottles is inexorably linked to territorial exclusivity and store-door delivery of each bottler's entire package mix, and the belief expressed by several bottlers that chain store outlets would substantially reduce, if not eliminate, their refillable bottle purchases if warehouse delivery of other types of packages were offered to them. Respondents' scenario projects a decline in the volume of soft drinks packaged in refillable bottles and distributed via store-door delivery and, as a result, price increases to cover fixed costs at the reduced volume. (Ans. Br. at p. 57).

While the record shows that a few high-volume chain stores have refused to retail returnable bottles (Tr. 2170–72, RPF 135–46)[56], we find no basis in the record for concluding that a [61] substantial segment of the nation's chain store population will follow this lead. According to the bottlers, some chain store customers complain about the handling costs associated with storing and sorting empty bottles (RPF 136), but respondents submit that the retailers take a markup sufficient to compensate them for their trouble, and there is no indication that the profit on returnables is not comparable to that which is made on nonreturnable bottles and cans. (RPF 132, 137).

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[56] The record shows, for example, that in Coatsville, Pennsylvania, several food chains have declined to handle returnable bottles (RPF 143), but the bottler in that territory not only offers returnable bottles, he offers his 10-ounce returnable bottles of Coca-Cola for $1.10 less per case than his 10-ounce nonreturnables (RPF 209, Tr. 2149); and despite the refusal of the chain stores to retail this type of package, he is planning to introduce the 32-ounce returnable, resealable bottle. (Tr. 2171). Similarly, in Reading, Pennsylvania, four large chain stores do not carry returnables, yet 16-ounce returnable bottles, priced on a per-ounce basis, were 61 percent cheaper in that territory than Coca-Cola in 12-ounce cans. (RPF 208). In Albany, New York, no chains carry Coca-Cola in returnable bottles, but the package is available in that territory. (RPF 143).

Apparently, the refusal to retail this package is a competitive decision, and in view of the uncontroverted evidence that the wholesale price for returnable, refillable bottles is usually cheaper than nonrefillables, the retailer who rejects the former may be less price competitive as a consequence. (Tr. 1771–73). Although some retailers may justify the disadvantage, many more likely will not.

As the record shows, demand for returnables has increased and stabilized in recent years at about 55 percent of "Coca-Cola's" nationwide can and bottle statistical sales volume[57], and while the percentage varies from territory to territory, returnables are a significant factor in virtually every territory surveyed in this record. (RPF 348). We therefore find it difficult to conclude that most high-or low-volume soft drink retailers who now handle the package would ignore this demand by declining to offer consumers the choice between convenience and economy packaging. [62]

Furthermore, while numerous bottlers subscribe to the contention and therefore conclude that returnable bottles could not be offered competitively in a split-delivery environment of store-door distribution and central warehousing, their testimony is largely based on speculation. (*Compare* Tr. 3575–76). Only two of the Coca-Cola bottlers who testified in this proceeding ever experimented with split-delivery of Coca-Cola, and their testimony shows that chain stores which have obtained central warehouse delivery of Coca-Cola in cans have continued to purchase it in bottles delivered directly to their retail outlets. Thus we find unwarranted the assumption that high-volume accounts will disappear from store-door delivery routes. (*See also* Text at 74–76 *infra).*

Moreover, the efficiency of a store-door route depends upon such factors as the number of customers on the truck route, the volume of soft drinks delivered to each customer, the distances between customers, and the time required to make each delivery. These factors may vary greatly on different routes, in different territories, in various competitive situations.[58] Consequently, a bottler can achieve delivery efficiencies by adjusting the type of accounts serviced on each route by each of his trucks. Such route adjustments are not unknown in the industry. (Tr. 4044).[59] Bottlers are, for example, flexible in adjusting their routes in response to fluctuation in demand for soft drinks caused, for example, by seasonal variations (Tr. 2567, IDF 38, Stip. No. 3, CX 1244G, Tr. 476) or by the addition of piggybacked brands which they [63] may distribute to customers who are located beyond the limits of their primary territory. (*See* Tr. 2848–56, 3064–69). In addition, delivery costs may be reduced by route adjustments which eliminate deliveries to unprofitable accounts or by establishing a minimum volume which the bottler will deliver to a customer's place of business. (*See* Tr. 1932, 2554). We recognize, of course, that some territories may be too small and the returnable bottle volume too insubstantial to allow a bottler to operate efficiently. A similar problem exists under respondents' territorial system. Yet in such circumstances in which a bottler is unable to compete in returnable bottle sales, he may merge or consolidate his territory and plant with that of another bottler, as respondents now recommend to their small bottlers as a means of increasing their volume and efficiency. (Tr. 615). For these reasons, we conclude that territorial [64] restrictions which cover a bottler's entire package mix are not justified because part of the mix includes the use of refillable bottles.[60]

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[57] According to stipulated data, total food store sales of the Coca-Cola brand alone in 1960 represented the movement of 143 million statistical cases, including returnable bottles and nonreturnable bottles and cans. (RX 2Z–44). By 1971 these statistical case sales of Coca-Cola had grown to 327.9 million cases. If we assume that only half of the Coca-Cola food store sales volume in 1971 were sales in returnable bottles (Tr. 661, 777–78, 3633, 3653, 3755), Coca-Cola brand volume in returnable bottles alone was a little over 163.9 million statistical cases, exceeding by approximately 20 million statistical cases the returnable and nonreturnable food store package volume in 1960. (Tr. 3653).

[58] Under the present system, for example, virtually all products are distributed on a store-door delivery basis and costs vary from one territory to another. In Hartwell, Ga., the bottler's break-even point per delivery is four cases (Tr. 1870–71); in Coatesville, Pennsylvania, on his scheduled routes, the bottler's break-even point is five cases (Tr. 2191); in San Antonio, Texas, the bottler estimated that he broke even on deliveries involving about six cases. (Tr. 2554–55).

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[59] It has been suggested that central warehouse delivery would siphon away 50 percent of the store-door delivery volume in most territories. This assumption, however, is speculative. The record shows that chain stores, large independent supermarkets, and convenience stores which are serviced by warehouses for other food items, as a class of customers, account for about 20 percent of the total sales of the bottlers of Coca-Cola nationwide. Within various territories, the percentage varies. In Washington, D.C., this customer class accounts for about 27 percent of the bottlers' sales; in Herminie, Pa. about 20 percent; in Wilmington, about 33 percent; in Belmont, Calif. about 60–65 percent; in Westminster, Md., about 18–20 percent. (RPF 325).

We note, in addition, that the fact these customers are serviced by warehouses for other food items does not mean that all or any specific portion of their requirements for Coca-Cola would be centrally warehoused. (*See* Text at 75–77 with accompanying notes, *infra*.). For example, the percentage of the bottlers' sales volume which is packaged in refillable bottles and the large sizes of nonrefillable bottles may continue to be delivered store-door to the retail outlets of these customers. Consequently, that portion of the bottlers' total sales volume which may actually be centrally warehoused will probably be, in many instances, significantly less than the bottlers' total sales volume to the class of customers who are serviced by warehouses for other food items.

[60] As we previously mentioned, prior to 1955, finished Coca-Cola was packaged solely in refillable bottles. Respondents' practice now applies to the bottlers' entire package mix, of refillables and nonrefillables, and we considered the effects of the restraint in that context. Under our order, a market context will prevail in which intrabrand competition will be fostered in the sale of Coca-Cola and allied products packaged in nonreturnable containers. Under these circumstances, we believe the restraint, if limited to refillable bottles, is reasonable for the reasons discussed above. There is no occasion to determine whether the restraint, before the introduction of nonrefillables, was reasonable as applied solely to sale of Coca-Cola in refillable bottles prior to 1955.

We should emphasize that our finding of reasonableness here is also limited to the use of refillable bottles. We note, for example, that no evidence was adduced that intrabrand competition would unduly burden the use of refillable containers which may be used in pre-mix or post-mix systems. These pre-mix and post-mix systems, unlike the refillable bottles, remain with the retailer who dispenses the beverage. Thus, it is significant that respondent Coca-Cola successfully packages and sells its fountain syrup in refillable five-gallon stainless steel tanks (Tr. 3773), even though the fountain wholesalers are not confined by territorial restrictions. In fact, the recapture and return system for post-mix containers seems to work well in view of the fact that The Coca-Cola Company has found it unnecessary to impose a deposit refundable upon the container's return. (Tr. 3773–74). As a prophylactic measure against the imposition of the restraint in the future, our order will cover post-mix syrup sales and distribution.

B. "SMALL BOTTLERS"

Respondents contend that an order eliminating the territorial restrictions which they impose on their bottlers would result in a restructured, highly concentrated industry dominated by a few large bottlers. Reversing the thrust of their own argument that interbrand competition now places limits on the extent to which their bottlers, both large and small, may increase their prices, respondents assert, "in this concentrated economic environment (*i.e.*, an environment free of respondents' territorial restrictions) in which hundreds of small bottlers[61] had been forced out of business," wholesale prices would rise. (Ans. Br. 57). [65]

Respondents' concern about a market structure in which their bottlers are competing intrabrand in the sale of Coca-Cola and allied products is indeed a curious defense of territorial restrictions which allow one bottler to be the sole source of supply of these products to the customers within his territory. Contrary to respondents' assertions, the removal of the restraints would probably result in a substantial reduction in concentration as existing independent Coca-Cola bottlers expand geographically to encompass the previously captive retail outlets of other bottlers in areas they are now forbidden to penetrate. Rather than reducing competition and increasing concentration, the elimination of territorial restrictions will probably increase both actual and potential competition and decrease concentration.

1. *Territorial Restrictions as a Method of Protecting Small Business*

Respondents' protestations about concentration and the future structure of the industry aside, the thrust of their argument is predicated on the notion that small independent Coca-Cola bottlers would be unfairly disadvantaged by intrabrand competition. Numerous bottlers, particularly the smaller bottlers, testified that they were dependent upon the refuge of their territorial enclaves because intrabrand competition would force them out of business.[62] This assessment was, in [66] turn, based on several assumptions which were adopted in a series of important findings in the initial decision.[63] The judge concluded that without exclusive territories, large bottlers of Coca-Cola would drive smaller bottlers out of business. He further concluded that a Commission order lifting the territorial restrictions:

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[61] At the time of his testimony at the trial, the President of The Coca-Cola Company could not define the term "small bottler," and when asked by Judge Dufresne "what is a small bottler?" he testified: "Well, I don't know, sir . . . [w]e have never really tried to make such a definition." (Tr. 590–91). The term "small bottler" is, of course, a relative term. Subsequent witnesses noted that the relative size of a bottler may be measured by the population in his territory, his annual case sales of soft drinks, and the number of people he employs. (RPF 279). The Small Business Administration classifies a manufacturer with less than 250 employees as a small business. In 1974 respondents conducted a census of Coca-Cola bottlers, and of the 567 bottlers who responded, representing about 75 percent of domestic bottlers of Coca-Cola, 529 had fewer than 200 employees. (RPF 284). In this proceeding, however, the term "small bottler" has been used primarily as a reference which encompasses a number of factors, such as a bottler's sales volume, production capacity, proximity to central warehouse customers, and his access to capital resources, among others, which are said to give one bottler a competitive advantage over neighboring bottlers.

[62] It is a questionable hypothesis as to whether territorial restrictions promote the viability of small business in view of the fact that they necessitate survival for many small bottlers by merger, rather than growth by internal

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> . . . would be in direct conflict with the purpose of the Congress in enacting and in agencies administering the antitrust laws ". . . to perpetuate and preserve, for its own sake in spite of possible cost, an organization of industry in small units which can effectively compete with each other." *U.S.* v. *Aluminum Co. of America*, 148 F.2d 416, 429 (2d Cir. 1945).

We acknowledge this admonition that one of the underlying purposes of the antitrust laws is to protect and preserve small business; indeed, in *American Cyanamid*[64], the Commission noted that "This agency also has its very roots planted in that philosophy. . . ." Our previous decisions implementing this philosophy clearly indicate, however, that we have never condoned anticompetitive practices solely for the purpose of eliminating competition between large and small firms. We stated in *Procter & Gamble:*

> . . . it may be appropriate . . . to note Congress' concern with the preservation (of small firms), to the extent compatible with social and economic progress, of the fundamental benefits of a small-business, decentralized economy. The interest of fostering equality of opportunity for small business and in promoting the diffusion of economic power . . . was unquestionably intended by Congress to be relevant in any scheme for the enforcement of Section 7. (63 F.T.C. 1465, 1555–56 (1963)).

[67] But in effectuating this policy, the Commission made clear that it does not subordinate "the protection of *competition* to the protection of small business *competitors.*" (Id. citations omitted; *Compare* Ans. Br. at 66–67). "Otherwise," as the Third Circuit has observed in another context, "what is intended as a shield for small competitors becomes a sword against the consumer." *NBO Industries Treadway Cos., Inc.* v. *Brunswick Corp.*, 523 F.2d 262, 279 (3rd Cir. 1975), *vacated on other*

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expansion. Between 1968 and 1971 there were 107 bottling plant mergers among Coca-Cola bottlers. (Tr. 650–51). In addition, respondent Coca-Cola has issued 14 temporary marketing bottler agreements, pursuant to which bottlers who have discontinued production continue to distribute, within their territories, Coca-Cola produced for them by neighboring bottlers. (CX 1245 A–M, CX 1246 A–J). When these agreements expire, The Coca-Cola Company does not intend to renew them. (Tr. 900). The marketing bottlers will then have the option to resume bottling or merge their territories with some other bottler. (Tr. 901).

According to the President of The Coca-Cola Company, the demise of small independent units of production under its system is a function of improvements in transportation, economies of scale, shifting population, changing tastes, and income patterns which "have tended to reduce the number of bottling plants and increase the size of some territories." (Tr. 614). In circumstances in which bottlers are too small to operate efficiently and foreclosed by territorial restrictions from significant internal expansion, respondents recommend that they merge or consolidate their production with another bottler (Tr. 615; *see also* Tr. 900–01), thus reducing the population of small bottlers.

[63] *See* IDF 185–193.

[64] 63 F.T.C. 1747, 1857–58 (1963).

grounds and remanded, Brunswick Corp. v. *Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 1977–1 Trade Cases, ¶61,255.

Consistent with our prior application of these principles, we conclude that territorial restrictions are not justified as a means of protecting small independent Coca-Cola bottlers from large independent intrabrand rivals, but that ancillary relief is necessary, in the public interest, to prevent The Coca-Cola Company's integrated bottling operations from exploiting certain advantages which may accrue to it as a dual-distributing trademark licensor.

a. Large Independent Bottlers v. Small Independent Bottlers

Recognizing that all of the bottlers who testified in this proceeding were concerned about intrabrand price competition within their respective territories, respondents and the bottler intervenors also adduced evidence from which it may be concluded that respondents' territorial policy is today the chief reason why many bottlers remain small. With access barred to retail accounts in densely populated areas now under the lucrative intrabrand domain of the metropolitan bottlers, expansion by a small bottler largely depends, absent a territorial merger, on population growth in his territory and per capita consumption of his product. Under these circumstances, large bottlers in the nation's major cities may be the principal benefactors of the "special protection" these restraints afford. (Tr. 872).[65]

The record shows that small bottlers, in some instances, may have overall cost advantages because, among other reasons, they have lower labor and land costs and lower taxes than large bottlers located in major metropolitan areas. (RPF 191, 290; *see* Tr. 2248, 2363). In fact, wholesale prices charged by large bottlers with high-speed, high-volume production facilities are often higher than the prices charged by small bottlers in adjacent territories. (RPF 295; Tr. 2179–80, 2832). Respondents submit this pricing behavior as evidence that many small bottlers may actually be more efficient overall than large [68] bottlers. (Ans. Br. 82; RPF 295, 188).[66] This evidence adduced by respondents

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[65] In one instance noted in the record, territorial restrictions prevented a small Coca-Cola bottler from doubling his annual volume by selling canned Coca-Cola to a customer who intended to tranship out of the small bottler's territory. (Tr. 665–66).

[66] Although the record is silent with respect to the bottling or canning plant volume necessary to achieve full economies of scale, bottlers who have merged their geographic markets and consolidated their operations testified that they have improved their bottling line efficiency. According to respondents' expert, however, the relative economies of production between large and small bottling plants are not a "big factor" in the soft drink bottling business. (Tr. 1044). With respect to canning operations, the production efficiencies of large canning lines average 3–5 cents per case (Meyers 1787–88), and this obviously may be a significant competitive factor. (*See* Tr. 3179).

However, nothing in the record suggests that economies of scale are any different for Coca-Cola bottlers than they are for Pepsi-Cola bottlers. Thus it is relevant, in assessing the relative advantage scale economies afford firms of different size, that "small" Coca-Cola bottlers effectively compete with "large" interbrand bottlers. The bottler in Hartwell, Ga., for example, has an annual sales volume of about 340,000 cases in a territory serving 35,000 people (RPF 280, 283); yet he apparently suffers no overall cost disadvantage despite the fact that Pepsi-Cola is sold in his territory

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from bottler witnesses tends to contradict their argument that small bottlers as a class would be unable either to defend their existing sales volumes or expand out of territories in which low costs and prices prevail into the territories of large bottlers who may be incurring higher costs and charging higher prices as a consequence. (*See* RPF 188, Tr. 881–86). Certainly, no prudent retailer of Coca-Cola and the allied products would continue to patronize a large bottler exclusively if he were able to purchase all or a portion of his products at a lower price from a competing **[69]** supplier. (*See* Tr. 3179).[67] In effect, then, territorial restrictions may, in some instances, be preventing small bottlers from fairly exploiting the competitive advantages which, in open markets, would ordinarily accrue to those who offer lower prices.[68] **[70]**

2. *Competition for the Business of the High-Volume Chain Store Accounts*

Although the judge found that small bottlers are often located near large bottlers (IDF 186), he also found that large bottlers in metropolitan markets would have a competitive edge over small bottlers for important central warehouse accounts "because chain store warehouses are located mainly in territories of large bottlers." (IDF 185; RPF 329, 333). At the outset, reject the notion that trade-

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by a bottling operation of General Cinema Corporation, which "owns North Georgia — and most of Florida." (Tr. 1390–93; *See also* Tr. 1671A–73). In a reverse situation, the viability of small Pepsi bottlers apparently was not threatened despite the fact that their territories were encompassed by the territory of the huge Coca-Cola Bottling Co. of New York. (Tr. 2276–78).

[67] The judge found that small bottlers do not have the production capacity to compete effectively for the business of the large chain store accounts.

Yet not only is the record unclear concerning the output capacity which would be required to serve all or part of the demand of large retailers from time to time, the finding ignores the fact that a bottler's ability to supply large-volume accounts does not necessarily depend on his in-house production capacity alone. Bottlers have, in the past, supplemented their production capacity by entering into agency canning agreements with contract canners (Tr. 837–38, *see* Tr. 3153–54), and as the record shows, the canned product is ideally suited to central warehousing. (*supra* fn. 25). Nothing in the record suggests that these canners could not produce canned Coca-Cola for small bottlers at prices which are competitive with the in-house canning lines of large bottlers. (*Compare* Ans. Br. 63, Fn. 70; Tr. 1325–26). Nor is there any evidence in this record which would suggest that those retailers which presently backhaul private label soft drinks produced for them by contract canners would not, except where local union contracts prevent it, backhaul Coca-Cola directly from a contract canning plant to the chain store warehouse.

In addition to contract canning as a means of boosting the capacity to supply a product, the record also shows that small bottlers can overcome capital barriers by joining together in cooperative soft drink canning ventures, such as the Mid-Atlantic Canning Association owned by 16 bottlers, including many small bottlers. (Tr. 2138, 2923–25, 1500, 1561, 1771–73, 2042). In these ways, small bottlers have arranged for additional production capacity to meet the demands in the markets they serve. Should the demand for the small bottler's product increase, the barriers would not appear to be insurmountable for those who attempt to accommodate it.

[68] The administrative law judge concluded that small Coca-Cola bottlers would not have the financial resources to meet the price reductions intrabrand competition may stimulate. While numerous bottlers did, in fact, express concerns about the financial resources of their neighbors, the record also shows that "small" bottlers have been able to price compete with larger, so-called deep-pocket interbrand bottlers serving customers within the small bottlers' territorial boundaries. As in many sectors of the economy in which large and small businesses compete, it is the large firms which usually possess the greatest financial resources, if not superior efficiencies. The soft drink bottling industry is no exception. But the disparity in the financial strength among various firms in a market is not, by itself, an accurate indicator of the ability of any particular firm, large or small, to compete effectively in the market.

restrictive territorial practices can be sanctioned as a means of eliminating fair advantages which may accrue to a bottler by virtue of his proximity to customers.

Beyond that, we find little in the record to support the judge's sweeping conclusions in IDF 185. While several bottlers testified that many chain store warehouses are located within the present territorial boundaries of large bottlers, there is scant evidence reflecting shipping distances or the relative "proximities" of large and small bottling facilities to the various chain store warehouse facilities. In fact, food store warehouses which may be located on the outer fringe of the territory of a large urban bottler could actually be closer to the production plant of a small suburban or rural bottler than the plant or distribution facility of the bottler in whose territory the warehouse is actually located. (IDF 186). The judge cited evidence indicating that the Baltimore Coca-Cola bottling facility of The Coca-Cola Company may be closer to an A & P warehouse than the bottling facility of the Westminister, Maryland, Coca-Cola bottler. (IDF 188).[69] But neither this example nor the fact that some central warehouses may be located within the territories of some large bottlers, but at undisclosed distances from bottling plants or distribution centers, supports a general conclusion that because of transportation disadvantages, [71] small bottlers would be unable to compete effectively for the business of high-volume retailers. The bottlers' prices are influenced by many factors, including their overall costs. As a result, a bottler who enjoys, by virtue of his location, a delivery-cost advantage with respect to one customer may be disadvantaged by his location vis-a-vis another bottler and other customers or by cost disadvantages he may incur in other aspects of his operation.

a. Central Warehouse Delivery and Backhauling by Central Warehouse Customers

Furthermore, the judge ignored the fact that respondents' territorial boundaries are no measure of the distances finished soft drinks may be shipped economically. Small bottlers presently haul and backhaul Coca-Cola efficiently from their bottling or coopeatively owned canning plants to their distribution facilities,[70] and they often transport the

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[69] In contrast with the testimony of the former president of respondent's bottling operation in Baltimore, cited in IDF 188, the small 7-Up/RC bottler in Herminie, Pennsylvania, testified that he has two potential warehouse customers in his territory which are located 20–30 minutes from his plant, but one hour from the plant of the large bottler of 7-Up and Royal Crown Cola in Pittsburgh. (Tr. 2823, *But see* Tr. 1783–84).

[70] For example, the 7-Up/Royal Crown bottler in Herminie, Pa., also owns the 7-Up franchise in Wheeling, W. Va. He testified that he ships soft drinks packaged in 28-ounce nonreturnable bottles from his Wheeling facility to his Herminie facility on a route which passes through the territory of the large Pittsburgh bottlers; however, because of the restrictions imposed upon his territories, he may not sell soft drinks at wholesale in the Pittsburgh territory. While this bottler would not consider it feasible to sell returnable bottles in Pittsburgh because of the problem of recapturing

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canned and bottled products produced for them by contract canners or other bottlers under agency arrangements over routes which sometimes traverse the territories of large neighboring bottlers. It is therefore likely that sizable portions of a large bottler's territory, and the customers within it, may lie within an area which small neighbors might effectively service.

Moreover, while backhauling by high-volume soft drink retailers from the canning plants of contract canners to their central warehouses is a customary mode of private label soft drink distribution (Stip. No. 7, Tr. 2998),[71] respondents [72] discount its importance as a means of distributing Coca-Cola and allied products. They claim the chain store trucks servicing the retail stores in the territories of small bottlers could not feasibly backhaul Coca-Cola from the bottlers' plants. The judge below agreed with this contention. Relying upon respondents' proposed finding of fact, he cited three witnesses in support of the conclusion that a small bottler could not supply chain store warehouses by allowing backhauling "because the chain store truck servicing the few stores in that territory would not have enough room to pick up a significant supply on a backhaul." (IDF 188).[72] We find the reference to "significant supply" vague in this context,[73] but assuming it relates to the bottlers' sales volumes, the testimony upon which it is presumably predicated is hardly a compelling basis for the finding.

Mr. Rooks, the Coca-Cola bottler in Hartwell, Georgia, testified that the chains may have "space problems" on the trucks which deliver to the retail chain outlets in his territory (Tr. 1417); and Mr. Christian, the President of the Charlottesville, Virginia, Coca-Cola Bottling Works, testified that he thought the chain stores could backhaul on the trucks they use to service their outlets in his territory, but he assumed the chain store trucks were, in fact, already backhauling other items. (Tr. 1843). Despite these assumptions, neither of these witnesses testified concerning the number of trucks servicing the chain outlets in

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the empties (Tr. 2849–50), he testified that it would be feasible for him to sell nonreturnable bottles in Pittsburgh (Tr. 2853–54), although if he did so, he would expect the bottlers there to respond by competing for customers in his territory. (Tr. 2855).

[71] In one instance noted in the record, canned Coca-Cola is being backhauled by a bottler's customer. The Alpha-Beta chain in Los Angeles is presently backhauling canned Coca-Cola from the Los Angeles Coca-Cola bottler to its central warehouse and subsequently transshipping it in its own trucks to Alpha-Beta retail outlets located in the territories of neighboring Coca-Cola bottlers. (Tr. 2584–85, 2588, 2634, 2650–51).

[72] *Compare* IDF 188 *with* RPF 333.

[73] It is unclear whether this finding refers to a supply of soft drinks which chain store customers might consider "significant" or a sales volume which the bottler would consider significant. However, no chain store customers were called to testify at the trial, and the record does not show what quantity of soft drinks any retailer would consider significant on a backhaul, although presumably a customer interested in backhauling from a particular bottler might consider, among other factors, how far removed the pick-up point is from the delivery truck's normal route, the quantity of soft drinks it requires and the bottler has available, and the price at which the soft drinks are being offered.

their respective territories; the frequency of the chain store deliveries to these [73] outlets; the amount of space, if any, which might actually be available on these trucks from time to time; or the amount of space the bottlers thought they would require to permit the backhauling of a "significant" volume of soft drinks.[74] The third witness cited by the judge, Mr. Roadcap, President of the Westminster, Md., Coca-Cola Bottling Company, doubted that backhauling would be feasible for reasons entirely unrelated to speculations about truck capacities in backhaul situations. [74] Mr. Roadcap stated that, backhauling would not be feasible because other Coca-Cola bottlers would find out that he had allowed Coca-Cola to be shipped into their territories, and in his judgment, "they would keep cutting the cost and it would go down, down, down to the point no one would make money. . . ." (Tr. 2459).

Whether backhauling would always be feasible for all of respondents' bottlers and their customers cannot be gleaned from this record, but neither was it complaint counsel's burden to disprove respondents' contentions that individual backhaul situations, in some cases, might not be feasible. Absolute competitive equality among bottlers was not a prerequisite of their case. The fact that a particular delivery mode may not be feasible for some does not justify a restriction which virtually precludes all bottlers from freely using it.

b. Store-Door Delivery to Central Warehouse Customers

While instances in which respondents' bottlers have offered delivery services other than store-door delivery are, as a consequence of respondents' efforts to preserve their territorial arrangements, admittedly rare, actual warehouse delivery situations are not unprecedented even within respondents' bottling network.[75] And limited though this experience may be, it shows that bottlers can provide, and their customers have accepted, both warehouse delivery of Coca-Cola in certain types of packages, such as cans, and store-door delivery of [75] Coca-Cola in bottles.[76] Indeed there appears to be a significant market among high-volume retailers for various delivery options. As a consequence, the competitive opportunities for small bottlers in open markets include not only the business which might evolve from central warehousing, but also the store-door trade to chain store outlets both within and outside their present territorial borders.

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[74] In finding 188, the judge, relying on the testimony of Mr. Hornsby, Executive Vice President and Treasurer of the K-S Canning Co., noted that an empty tractor trailer truck can accommodate 1800 to 1900 cases of 12-ounce cans. (Tr. 3175). (Both respondents' proposed finding of fact No. 333 and the judge's finding of fact IDF 188 erroneously cite Mr. Meyers, former President of Shasta Beverages, as the source of this statement.) While accurate in substance, the context in which this fact is used in IDF 188 seems to suggest that a tractor trailer truck, if used by a chain store to deliver other food items to retail stores in a bottler's territory, could not, even if empty, backhaul "significant" supplies of Coca-Cola. Considered in light of other facts presented at the trial, the first two findings in IDF 188 lack the scope necessary to give them any realistic perspective.

Recognizing that we cannot, on this record, state definitively the chain store backhaul capacity, if any, which may be available to individual bottlers, we note that if one empty tractor trailer truck, or its equivalent from partial truckloads backhauled by several customers, were available to a bottler once a week, for example, it would provide a backhaul capacity of approximately 100,000 cases of cans annually, or the equivalent volume of about 150,000 statistical cases of 24 8-ounce bottles. We note further that the record shows this would be more than sufficient to haul the total annual soft drink volume many small bottlers now sell to chain store customers. (*But see* fn. 59 *supra*).

Mr. Rooks of Hartwell, Georgia, for example, had total sales of 340,000 statistical cases (Tr. 1422, RPF 283), but only 25 percent of his sales went to customers with warehouse facilities. (Tr. 1371, 1438; RPF 325). Consequently, a backhaul capacity of about 85,000 statistical cases would maintain his sales volume to chain store customers.

Similarly, while Mr. Roadcap's testimony about the feasibility of backhauling was concerned with other matters, the record shows that he has total sales of about 500,000 statistical cases (Tr. 2434-35, RPF 283), but only 20 percent of his total represented sales to customers which are served by warehouses for other food items. (Tr. 2436, 2438; RPF 325). An annual backhaul capacity of 100,000 statistical cases would maintain his sales volume to chain store customers.

3. *Store-door Delivery to Customers Without Central Warehousing*

The record further shows that many small bottlers would, absent territorial restrictions, have access to huge metropolitan markets in which thousands of soft drink retailers not serviced by central warehouses for other food items presently obtain Coca-Cola and allied products on a store-door delivered basis. While chain stores, large independent supermarkets, and convenience stores serviced by warehouses are important to [76] the bottlers (RPF 325), in the largest metropolitan areas, as much as 73 percent of the bottlers' volume is delivered on a store-door basis.[77] (Tr. 2309–09). Although a part of this volume may represent sales in refillable bottles, the exclusivity of which will remain undisturbed, store-door delivery of nonrefillable containers in these metropolitan areas still holds substantial opportunities for growth and market expansion by small bottlers.

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[75] The record shows that in the early '60s a group of Coca-Cola bottlers on the west coast entered into a cooperative agreement for the purpose of experimenting with warehouse delivery of Coca-Cola in cans through the Safeway, Lucky, and Purity food chains. According to respondents and the bottlers, these experiments failed. While the bottlers were apparently dissatisfied with the way some store managers at the retail outlets were merchandising the product after the chains had purchased it, it is arguable that merchandising decisions in individual retail outlets, such as the number of shelf-facings a product will receive in a store, are not misplaced if left to the discretion of the retailer who buys the product for resale.

Nor does the record show that these experiments demonstrate the failure of split delivery. The tests lasted several years during which time, participating customers who picked up Coca-Cola in cans from the canning plant and backhauled it in their own trucks to their respective warehouses (Tr. 2623) still purchased bottled Coca-Cola from individual bottlers for store-door delivery to the chain store retail outlets. (RPF 110). Although respondents claim such delivery is infeasible, these early tests with central warehousing involved split delivery to a significant degree. Nor are they of purely historical significance.

As we noted previously, the record shows that the Alpha-Beta chain receives at its warehouse canned Coca-Cola which it obtains from the Los Angeles Coca-Cola bottler and transships into the territories of neighboring bottlers; Alpha-Beta, however, still purchases Coca-Cola in returnable bottles delivered store-door by the bottlers in the territories in which its retail stores are located. (Tr. 2584–85, 2588, 2634, 2650–51; *See also* Tr. 3575–76).

[76] On the large size bottles, for example, store-door delivery may be more efficient than central-warehouse delivery. (Tr. 3438–39).

[77] For example, in New York about 70,000 accounts purchase Coca-Cola; in Washington, D.C., 15,000 accounts purchase it; 6,400 accounts purchase it in Richmond; 12,000 accounts purchase it in San Antonio, Texas; and 3,000 accounts purchase it in Wilmington, Delaware. In contrast, the small bottlers in Annapolis, Maryland, and Charlottesville, Virginia, service 1,335 and 1,375 accounts respectively. The bottler in Westminster, Maryland, services a total of about 1,000 accounts and the Coatesville, Pennsylvania, bottler services about 1,200 accounts. The Dover, Delaware, bottler services a total of about 650 accounts while the neighboring bottler in Wilmington services about 300 Mom and Pop stores alone. (RPF 225).

Respondents correctly assert that in the absence of exclusive territories, a big bottler may compete intrabrand for the relatively few accounts the small bottlers presently serve, but the potential for a small bottler to expand might include thousands of accounts now foreclosed to him.

4. *Territorial Restrictions Foreclose Fair Intrabrand Competition in the Sale of Coca-Cola and Allied Products Packaged in Nonrefillable Bottles and Cans*

While larger and potentially more fertile markets would, absent the restraint, open to small bottlers, we acknowledge that the free market provides no assurance that all of respondents' bottlers will compete effectively or thrive in an unsheltered environment.[78] Nevertheless, we reject respondents contentions that the antitrust laws embody a pledge to protect [77] small bottlers from competitive risk and that The Coca-Cola Company may redeem the pledge by keeping captive the demand side of a market which includes soft drink retailers from coast to coast and indirectly the consuming public served by those retailers.

Respondents simply misapply the thrust of our decisions and those of appellate tribunals directed toward the preservation of small business. The precedents respondents invoke, for example, involve situations in which anticompetitive behavior, such as monopolization[79], merger activity[80], exclusive dealing-type franchise arrangements which impede independent franchisees from purchasing supplies from their franchisor's competitors,[81], boycotting[82], and discriminatory pricing or promotional practices in violation of the Robinson-Patman Act[83], were condemned by this Commission or the courts. These cases, to the extent they implement the concern of Congress for the preservation of small business, demonstrate a strong public policy to protect small business, not from open and fair competition, but from unfair anticompetitive acts and practices of larger rivals. In essence, the decisions concerned with small business problems issued by appellate tribunals share in common the singular proposition that small business may be shielded from the unfair, anticompetitive practices large firms sometimes

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[78] We noted previously that many small bottlers have been locked into territories that are so small they cannot generate enough volume to support an independent bottling operation. Thus the number of small bottlers forced to merge with or sell out to neighboring bottlers is substantial. The record shows that the survival of the independent small business unit of production and distribution of Coca-Cola and allied products is, under respondents territorial system, threatened in numerous instances by inescapable inefficiency due to their confinement in small territories. (Tr. 615, 895–901).

[79] *U.S.* v. *Aluminum Co. of America*, 148 F.2d 416 (2d Cir. 1945).

[80] *F.T.C.* v. *Procter & Gamble Co.*, 386 U.S. 568 (1967); *Brown Shoe Co.* v. *U.S.*, 370 U.S. 294 (1962); *National Tea Co.*, 69 F.T.C. 226 (1966).

[81] *Brown Shoe Co.*, 62 F.T.C. 679 (1963).

[82] *Fashion Originators' Guild* v. *F.T.C.*, 312 U.S. 457 (1941).

[83] *F.T.C.* v. *Fred Meyer, Inc.*, 390 U.S. 341 (1968).

employ against them, but the case law is equally clear that the antitrust laws afford small business, as a class, no license to engage in anticompetitive market segmentation activity for its own protection (*See Topco, supra);* nor do we find in them sanction for the patronage of respondents' anticompetitive activities, presumably on behalf of the small bottlers.

The threat of competitive confrontation between large and small independent bottlers is alone not enough to justify the imposition of a restraint preventing consummation of the threat. To conclude otherwise would, in our judgment, clearly represent a novel departure from free market principles; neither the precedents cited by respondents and the judge nor the circumstances revealed in this record lend any support for it. [78]

5. *Independent Bottlers v. The Domestic Bottlers' Subsidiaries of The Coca-Cola Company (DBS)*

Intervenors' most vigorous objections to an order lifting territorial restrictions concern the competitive imbalance which they assert might exist between the independent bottlers and The Coca-Cola Company's DBS operations. Intervenors contend that The Coca-Cola Company, as a dual-distributing trademark licensor, may have critical advantages over its bottlers, unrelated to the efficiency of its syrup-producing and bottling integration. We have carefully considered the evidence relating to the competitive imbalance which intervenors perceive.

a. Respondents' Access to Confidential Trade Information

The record shows that the The Coca-Cola Company, in the course of its business as a trademark licensor and syrup supplier, acquires detailed and sensitive, competitive information about each of its bottler's business operations. For example, during routine quality control inspections of bottling plants, respondents can obtain access to the type of information which may reflect a bottler's production capacities and competitive capabilities, including the innovations and methods a bottler may employ to reduce his production-line or plant costs, or increase his capacity and competitive potential.[84] In addition, a bottler must obtain The Coca-Cola Company's approval before using new, previously unauthorized types of packaging, and as the record amply demonstrates, packaging decisions in this industry can be a vital aspect of a bottler's marketing strategy. (RPF 253). The Coca-Cola Company would have advance knowledge of, and the right to approve, new packaging innovation and, unlike its independent bottlers, could begin to react to a bottler's innovation before it was actually introduced into the market. **[79]** The sensitivity of this type of information is further evidenced by the fact that The Coca-Cola Company itself argued persuasively for *in camera* treatment in this proceeding of similar types of commercial data in order to prevent it from falling into the hands of syrup company competitors and their bottlers (Tr. 486–87; CX 1–2, *in camera*), and complaint counsel agreed the request was not "wholly without merit." Thus it appears that, as trademark licensors, respondents' relationship with their bottlers is more in the nature of a fiduciary than a competitor. (Tr. 487). Under these circumstances, we believe it would be inequitable and unfair to ignore intervenors' concern that the bottling operations of the trademark licensor may easily obtain access to competitively sensitive information and may easily exploit the advantages this would give them.

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[84] While it may have, in the past, been beneficial to the overall efficiency of the Coca-Cola and allied product bottling network for each bottler within it to pass on useful commercial information to other bottlers, such efficiencies may not be possible and may have to be sacrificed to some degree in the interest of preserving the free market. In these circumstances, as Bork has observed, a manufacturer:

> . . . is much less likely to make known to others in the system any particularly successful selling or manufacturing techniques it devises if there is a substantial possibility that such techniques will be used to take business away from it. (Bork, *The Rule of Reason and the Per Se Concept: Price Fixing and Market Division*, 75 Yale L. J. 373 (1966) at 439–40.

If a firm cannot be protected by a market division agreement from the danger of the "free rider," it probably would, in its own interest, cut off the information flow. (*Id.* at 445). Certainly an independent bottler would not,

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Our order will, therefore, require respondents to safeguard the information they acquire from their independent bottler licensees in the course of respondents' business as trademark licensors and syrup suppliers. Disclosure of this type of information to those of respondents' employees involved in or responsible for the production and sale of finished soft drinks will be prohibited. Respondents will also be enjoined, pursuant to paragraph II F. of our order, from enforcing or aiding in the enforcement of plant inspection provisions incorporated into licensing agreements, which respondents have approved or consented to, between any bottler and the bottler's sub-bottlers, term sub-bottlers, or temporary bottlers. (*See, e.g.*, CX 20B Para. (f), CX 35C Para. (f), CX 36D Para. (f)). This provision is necessary to prevent exploitation and competitive abuse of information which may be acquired by bottler/licensors, and should impose no undue **[80]** burden upon respondents' quality control program in view of the fact that respondents retain the right to inspect the sub-bottlers' facilities, and the further fact that respondents customarily conduct inspections of

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voluntarily, yield his production and marketing ideas and strategies to any direct competitor. It is true that much of the data, such as monthly sales to chain stores and planned promotions, is apparently supplied voluntarily by independent bottlers to The Coca-Cola Company. This type of data presumably could be withheld if it were in the bottlers' interest to do so. Other types of information, however, concerning the independent bottlers' plant facilities and production capacities, for example, would as a consequence of the trademark licensing relationship, be extremely difficult for the bottler to withhold or safeguard.

every plant at which soft drinks bearing their trademarks are produced. The injunction will, however, include an exception which will allow respondents to continue to fill orders for finished packaged soft drinks from licensed Coca-Cola and allied product bottlers pursuant to agency bottling or canning agreements.

b. Divestiture Stipulation

The bottlers also contend, however, that divestiture of integrated bottling operations by respondent Coca-Cola and other integrated syrup companies would be the only effective way of dealing with unrestrained dual distribution in this industry. (*See* Ans. Br. by Coca-Cola Bottling Company of Los Angeles, *et al.*, Para. at 33–34). The Coca-Cola Company and its bottlers have negotiated a stipulation pursuant to which respondent Coca-Cola has agreed not to object to a divestiture order, provided the Commission enters equivalent relief against seven other syrup suppliers.[85] Yet we cannot, in the abstract, endorse a proposal premised on remedies in cases not yet adjudicated; nor are we, on the record before us, prepared to decide a general rule of vertical divestiture, including situations possibly involving de novo entry or toehold entry by acquisition, which could rule out the potential efficiencies of integration as well as the potential procompetitive effects it may have in this industry. Certainly, nothing in this record demonstrates that such measures would be appropriate. To the contrary, although we reserve judgment on cases involving other syrup companies now pending before the administrative law judge, it is not inconceivable that vertical integration by acquisition or de novo entry into bottling might be justified by a smaller syrup company attempting to piece together a nationwide bottler distribution network to compete with [81] the industry giants such as The Coca-Cola Company and PepsiCo. (*See* Text at 12, fn. 14 *supra*). Nor is there sufficient independent record basis for extraordinary divestiture relief against respondents in this proceeding.[86]

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[85] The divestiture stipulation is limited by the following caveat:

> . . . the other seven manufacturers of nationally branded soft drink syrups against whom the Commission now has complaints pending and their subsidiaries and affiliates are required by the Federal Trade Commission, in Docket Nos. 8853 (Crush International, Limited), 8854 (Dr. Pepper Co.), 8856 (PepsiCo, Inc.), 8857 (The Seven-Up Co.), 8858 (The Royal Crown Co.), 8859 (National Industries, Inc.) and 8877 (Norton Simon, Inc.), to divest and do divest all other bottling, canning, and distributing operations. . . . (Tr. 4104–05; Stipulation No. 10, Docket Binder 1–3–3, filed June 27, 1975).

[86] Intervenors note that The Coca-Cola Company has the capacity to exploit its resources as a dual-distributing syrup producer for the purpose of increasing the market share of its bottling subsidiaries. Citing the testimony of John H. Ogden, Executive Vice-President of Coca-Cola U.S.A., intervenors point out that respondent's Chicago DBS has, since 1975, incurred losses because its management viewed that territory as "an area for investment spending, believing that leadership in a market ultimately moves to a profitable position." (Tr. 840–41). While intervenors emphasize that the profits of the DBS operations constitute approximately 1 percent of The Coca-Cola Company's pre-tax profits and that it might be economically feasible for respondent Coca-Cola to operate its DBS on a break-even basis for an extended period of time, no evidence was adduced at the trial that respondent provides deep-pocket

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The burden of establishing the necessity of ancillary relief, such as divestiture or supply limitations in the nature of convenants not to compete, rests with the party asserting the need for such protection. Frequently, this burden is assumed by government counsel in cases in which it appears that ancillary relief is necessary in the public interest to preserve the competition fostered by the primary remedies of antitrust litigation, *Ford Motor Co.* v. *U.S.*, 405 U.S. 562 (1972); *L.G. Balfour Co.* v. *F.T.C.*, 9 S&D 26, 56 (7th Cir. 1971); *Luria Bros. & Co., Inc.* v. *F.T.C.*, 8 S&D 615 (3rd Cir. 1968), by intervenors who seek to protect interests they believe will not be adequately represented by the parties, *Ford Motor Co.* v. *U.S.*, *supra*, or by plantiffs in private treble damage actions. *Brunswick Corp.* v. *Pueblo Bowl-O-Mat, Inc.*, *supra* at 70,775. But as the court observed in *Papercraft Corp.* v. *F.T.C.*, 9 S&D 530, 536 (7th Cir. 1973), ". . . divestiture orders have included special provisions designed to insure the survival of the divested business, but in each instance the supporting findings demonstrated the need for a special protective provision." No evidence of need for ancillary divestiture relief has been adduced in this case. [82]

c. Request for Further Hearings on Relief

The bottlers further argue that a remand on issues of relief is necessary if their interests are to be adequately protected. Intervenors had fair notice that issues of relief were before the judge. Intervenors were afforded every opportunity to participate in the development of the trial record; they were authorized to offer documents into evidence, to call witnesses to testify in their behalf, and to examine or cross-examine witnesses called by respondents and complaint counsel. Along with the 26 bottlers, representing a cross section of the industry, seven executives of The Coca-Cola Co., the former President of Shasta Beverages, the Executive Vice-President of K-S Canning Corp., a contract canner, and two representatives of canned ice tea producers appeared at the trial. As the record shows, these witnesses addressed issues of relief as well as issues of liability; and intervenors' counsel, present at each hearing session, were free to pursue with these witnesses lines of inquiry relevant to questions of relief at intervenors' discretion. The fact that the record now fails to support intervenors' theories concerning the need for ancillary protection, in all respects, is

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subsidies to its Chicago DBS or supports below-cost sales. As intervenors must fully appreciate, even independent bottlers sometimes operate unprofitably. (Tr. 1475). Evidence such as this hardly establishes the necessity for drastic ancillary divestiture relief. Nor are intervenors' other theories, analogizing this situation to vertical merger cases, supported by this record. *See Brunswick Corp.* v. *Pueblo Bowl-O-Mart*,——— U.S. ———, 1977-1 Trade Cases, Para. 61,255; *Elfman Motors, Inc.* v. *Chrysler Corp.* [567 F.2d 1252] 1977-2 Trade Cases, ¶ 61,650.

no basis for concluding that a remand of this proceeding is either justified or necessary.

Several intervenors also request consolidated, industrywide hearings on relief. While this seems to assume the liability of other respondents in proceedings involving rule of reason inquiries, still pending before the administrative law judge, the contention that such hearings are necessary is otherwise lacking in merit. For even if we momentarily assume, for the sake of argument, the liability of respondents in proceedings before the judge, it would not necessarily follow that uniform, industrywide remedies or uniform ancillary relief would be necessary or appropriate. To the contrary, fact records different from the record here before us may well justify different remedial provisions.[87] Under the circumstances, [83] we believe that a remand on issues of ancillary relief in consolidated, industrywide relief hearings is unwarranted and would unnecessarily delay final disposition of these cases.

C. NATIONAL ENVIRONMENTAL POLICY ACT (NEPA) CONSIDERATIONS

Finally, respondents contend that an Environmental Impact Statement (EIS) must be prepared by the Commission, pursuant to the National Environmental Policy Act (NEPA) (42 U.S.C. 4321, *et seq.*) before a final order is entered in this matter. Our rules provide that a formal EIS need not be filed in our adjudicatory proceedings. (16 CFR 1.82(d)). The issue has never been squarely before a court.[88]

At the trial, respondents called two experts on the ecological impact of beverage containers. These witnesses concluded that the returnable, refillable bottle may be an ecologically sound form of packaging. At two trips, for example, the refillable bottle has roughly the same impact on the environment (including water use, solid waste generation, air pollutants, water-borne wastes, and energy effluents) as the nonrefillable, nonreturnable bottle (Tr. 3801, RX 126Z20–23); at four trips it has about the same impact as the conventional steel can (Tr. 3801); at five trips its impact is about that of an aluminum can which is recycled at an 80 percent rate. (Tr. 3802). Evidence also suggests that the refillable bottle with a trippage of 10 is more energy efficient than steel or aluminum cans or glass, nonrefillable bottles.[89] Under certain circumstances, then, the returnable, refillable bottles may be ecologically superior to other package forms used by the bottlers. [84]

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[87] We note that respondents have vigorously opposed consolidated industrywide hearings. (Opposition of Respondents to Motion For Consolidation, Dkt. Binder 8855, 1–3–1, filed August 12, 1971; *See* Order Denying Motion To Consolidate Proceedings, filed September 29, 1971).

[88] *See Gifford-Hill & Co.* v. *F.T.C.*, 389 F. Supp. 167 (D.D.C. 1974) *aff'd* 523 F.2d 730 (D.C. Cir. 1975); *Mobil Oil Corp.* v. *F.T.C.*, 1977–2 Trade Cases, ¶61,632. The Council on Environmental Quality, whose interpretation of statutory requirements under NEPA is entitled to great deference (*Warm Springs Dam Task Force* v. *Gribble*, 417 U.S. 1301, 1310 (1974); *Jicarilla Apache Tribe* v. *Morton*, 471 F.2d 1275 (9th Cir. 1973); *Environmental Defense Fund* v. *Tennessee Valley Authority*, 468 F.2d 1164, 1177–78, (6th Cir. 1972)), has concluded that the Commission's Rule 1.82(d), exempting adjudicatory proceedings from the EIS requirement, was consistent with NEPA. (Brief for Defendents-Appellees, Addendum, Gifford-Hill, *supra*.).

We noted previously, however, that territorial restrictions on the use of returnable, refillable bottles will not, for reasons heretofore stated, be lifted by our order. As a result, a bottler will have even greater incentives than exist now to promote reusable bottle sales, since an increase in the intrabrand market share of this container will increase the bottler's soft drink volume protected by exclusivity. Nor would the "free rider" problem (*See* text at 32–35 *supra*) deter a bottler from actively promoting, as some have in the past, any economic and ecological benefits of the package in his territory. (RX 60, Tr. 2499). Use of refillable bottles is unlikely to change significantly as a result of the relief entered in this proceeding.

Beyond these observations based on the record compiled at the trial below, we note that NEPA was not designed to stymie the Commission's enforcement activities which seek to redress violation of the antitrust laws. Nor does NEPA, its legislative history, or its precedential case law require the preparation of a formal EIS in this proceeding. We find no basis for respondents' claim that these requirements apply to the adjudicatory activities of law enforcement agencies.[90] [85]

VII. CONSIDERATION OF THE DISSENTING STATEMENT OF COMMISSIONER CLANTON

In his dissenting statement, Commissioner Clanton recommends that this matter be remanded to the administrative law judge for hearings which would further explore the competitive effects of the challenged practice. The rationale which leads to this recommendation is, we believe, erroneous in two basic respects. First, it misapprehends complaint counsel's burden of proof. Second, it concludes that there is not enough evidence in the record to decide this case.

The dissent contends this case cannot be resolved without a full structural analysis of the soft drink syrup producing and bottling industries.[91] (Dissent p. 2). At the bottling level where the restraint precludes intrabrand competition, the undertaking recommended would include surveys of each territory to determine (1) Coke's market share, (2) concentration trends over time, (3) barriers to new entry and barriers to effective competition, (4) the degree of product differentiation, and (5) market performance and profitability of fountain syrups. In addition, after further discovery, a "rigorous analysis" of profitability at the manufacturer and bottler levels would also be required. (Dissent p. 21).[92] If, after examining the **[86]** structural characteristics of numerous territories, it can be inferred that bottlers possess substantial market power, this might justify "striking down the restrictions irrespective of any countervailing benefits." (Dissent p. 10).[93]

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[89] Little evidence was adduced concerning the environmental impact associated with litter attributable to the use of one-way, throw-away containers.

[90] We note further that NEPA requires preparation of an EIS only in connection with "major Federal actions significantly affecting the quality of the human environment. . . ." 42 U.S.C. 4332(2)(c). Based on our review of the record in light of that standard, we conclude that our order would not in any event require preparation of an EIS. Moreover, our decision, permitting respondents to continue their territorial restraints with respect to refillable bottles, is, we believe, less likely to have any effect on the use of this container than any resolution of this case other than allowing respondents to continue to restrain competition in violation of Section 5. NEPA, however, does not immunize respondents' unlawful activities, for environmental reasons, from the Commission's law enforcement processes.

The critical question raised by the dissenting opinion is whether complaint counsel, having demonstrated that respondents' vertical restraint adversely affects competition in the soft drink industry, were also required to adduce evidence showing the effect of the restraint on market shares and concentration, entry barriers, product differentiation, or the profits of the manufacturer and bottlers. We think not.[94]

We do not dispute, as the dissent suggests, that statistical data and market structure evidence might be relevant, and in some instances necessary, to determine the competitive effects of vertical restraints.

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[91] It should be noted the territories imposed by PepsiCo, Inc., challenged in a companion matter, are not necessarily co-extensive wtih the territories of the Coca-Cola bottlers in the "corridor area" and arguably would have to be separately surveyed.

[92] Responding to a note in the *Harvard Law Review*, the dissent suggests that "the indicia for measuring market power are familiar concepts which do not present unmanageable problems of proof in a rule of reason case." (Dissent p. 20).

The burden of the inquiry proposed by the dissent should not be underestimated. We know from experience in merger cases involving one or two geographic markets and similar structural inquiries that such litigation is complex, extremely time-consuming, and burdensome to all parties.

In this instance, the trial would begin again from scratch, extensive pre-trial discovery would be required, and the structural characteristics both of the syrup industry and the bottling level in numerous territories, each the equivalent of a separate geographic market, would have to be surveyed and litigated. In all likelihood, years of costly trial would ensue; this, we believe, is unnecessary.

[93] It should be noted that if it were established that a bottler had "substantial market power," the dissent would apply what is virtually a per se standard of illegality. It is unclear, however, whether this per se rule would prevent a new entrant, for example, at the syrup producing level, from offering exclusive territories in piggybacking situations to bottlers with market power. Whether market power evidence alone would be sufficient to meet the rigorous standards for applying a per se rule need not be decided.

[94] Economists sometimes use the terms "market power" and "monopoly power" interchangeably. *See* Scherer, *Industrial Market Structure and Economic Performance* (1970) at 10. The dissent notes that "The Commission determined correctly that proof of monopoly power or unrestricted market power, as argued by respondents, is an unnecessary prerequisite to a finding that a particular restraint is unreasonable." (Dissent p. 14).

In recommending a remand to adduce market power evidence, it is unclear whether the focus would be to determine the bottlers' market power in light of all the brands they may piggyback or just the Coca-Cola brand. (The dissent's analysis of the effect of piggybacking on entry barriers at the syrup-producing level, which we previously noted, *supra* at 49, fn. 45, is entirely consistent with our conclusion that piggybacking also tends to concentrate brands at the bottling level.) This is important because the focus of the remand sought by the dissent seems to be limited to a determination of the market power of Coca-Cola. Yet this would ignore the fact that piggybacking tends to concentrate brands and the power to price piggybacked brands in the hands of the strongest bottlers in a territory.

Yet, the adverse effects of the restraints in this case have been established without such evidence. The [87] record demonstrates that respondents' territorial policy (1) impedes competition in the types of delivery services bottlers offer to their customers[95], (2) prevents efficient bottlers from fully exploiting their competitive advantages, and (3) prevents retailers located within the territories of less efficient bottlers from purchasing Coca-Cola and allied products from efficient sources of supply. Moreover, the record leaves little doubt that the practice substantially lessens both intrabrand and interbrand price competition. The testimony of the President of The Coca-Cola Company, other officials of the company, and bottlers, which virtually constitutes admissions of substantial adverse competitive effects, clearly supports these findings.[96]

Such anticompetitive effects have indeed been inferred in cases where the evidence was much less direct than it is here. Relying on *U.S.* v. *Continental Can Company*, 378 U.S. 441 (1964), the Commission recently noted that concentration and market share data alone suffice to establish illegality of a merger in the absence of convincing proof to the contrary. *Jim Walter Corp.*, Dkt. 8986, issued December 20, 1977 [90 F.T.C. 671]. The evidence in this record that respondents' practice substantially lessens price competition is, we believe, more compelling than would be the case if such effect were inferred from concentration and market share data alone. The dissent, moreover, would require a more detailed evaluation of pricing patterns in the industry. As we recently noted, however, "The absence of discernible effect on pricing or the lack of small company failures attributable to a merger can be given little weight. . . . At best, such effects are difficult to measure, particularly if prices are already at non-competitive levels."[97] Adverse effect on price is, however, [88] clearly discernible in this record. Similarly, evidence, which the dissent would require, showing whether new entrants have made inroads into the various territories would be of limited utility in rebutting the evidence of anticompetitive effect reflected in the record.[98]

As we mentioned, a *prima facie* case was established through the testimony of the President of The Coca-Cola Company and other industry witnesses. Thus as Commissioner Clanton, writing for a unanimous Commission in the *Jim Walter* case, correctly observed, it is respondent's burden, once a *prima facie* case has been established based upon other evidence of anticompetitive effect, to provide exculpatory evidence "pertaining to the structure, history, and probable future of the asphalt and tar roofing industry sufficient to overcome the presumption (arising from concentration and market share data alone) that the merger threatens a substantial lessening of competition." (*Jim Walter Corp., supra* at 42, *et seq.)*. In this instance, we believe it was unnecessary for complaint counsel to resort to further statistical data to confirm the testimony upon which a *prima facie* violation of Section 5 had been established, and to the extent such data may have been relevant to the defense, it was respondents' burden to adduce it.

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[95] The reservations expressed in the dissent about the demand for central warehousing would certainly surprise the witnesses who testified in this proceeding. While the pros and cons of this method of distribution were hotly contested, the demand for the service was never seriously disputed. (RPF 88–91, Ans. Br. 55).

[96] The dissent without elaboration would dismiss, as "anecdotal," testimony reflecting the adverse effects of the practice provided by these witnesses in response to questioning by the judge and by counsel. We are unable to depreciate such testimony in this manner. (See Text at 27 fn. 28; 47–52 *supra*.)

[97] *Jim Walter Corp., supra.*

[98] *Id.* at 45–46. As we stated in *RSR Corp.*, 88 F.T.C. 797 (1976):

> even proof of low entry barriers . . . can be at most of slight exculpatory value in the face of probable anticompetitive effects, since all it suggests is that such effects may be smaller or short lived, not that they are unlikely to occur. (at 289).

Furthermore, *Jim Walter* clearly indicates that the burden of proof rests with respondent to show whether "new firms have eroded the market position of the industry leaders." (*Supra* at 46).

We agree with the dissent that ". . . one's preference for one kind of competition over another (price competition v. nonprice competition) should not automatically condemn" respondents' practice, although we believe that emphasis on the tendency of respondents' practice to impede price competition [89] is not misplaced. A practice which lessens price competition touches the core of the free enterprise system. The Supreme Court has described the price mechanism as "critical" and "sensitive." *U.S.* v. *Container Corp. of America*, 1969 Trade Cases at 86,413. In *U.S.* v. *Socony-Vacuum Oil Co., Inc.*, the court, citing Handler, *Federal Antitrust Laws—A Symposium* (1931), noted that this aspect of competition is "the central nervous system of the economy." Thus the alleged justifications for a practice which substantially lessens price competition requires, and in this instance has received, the closest scrutiny.[99] [90]

The dissent reexamines these justifications and raises a number of questions concerning whether investments by bottlers operating in exclusive territories enhance or impair competition, whether exclusive territories facilitate interbrand competition by enhancing availability[100] and by inducing greater demand for soft drink products, whether territorial restrictions facilitate advertising by the bottlers which promotes interbrand competition, and whether obstructions to intrabrand competition are necessary to maintain product quality. The issues now raised in the dissent, concerning which it finds the record inadequate, were previously raised by respondents in the form of affirmative arguments in justification of these restraints. In each instance, the evidence respondents relied upon in support of their contentions that the restrictions were reasonably necessary to maintain at current levels the interbrand viability of Coca-Cola and allied products were carefully examined by the Commission and found wanting.[101]

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[99] It is likely that the recommended surveys of various territories might disclose that some bottlers have "substantial market power" while others may not, and it is unclear what outcome the dissent would regard as appropriate in these circumstances. If a certain percentage of the bottlers surveyed possessed "substantial market power," would this justify striking down the restraint as it applies to the others "irrespective of any countervailing benefits?" If not, would the restraint be illegal only when it applies to bottlers with "substantial market power?" The surveys called for by the dissent might reveal, for example, that Coca-Cola bottler A has "substantial market power," but not Coca-Cola bottler B. Would the restriction then be lawful as applied to bottler B and unlawful as to bottler A? This would leave bottler A with "substantial market power" free to compete while bottler B would remain restrained. Yet in order to dissipate the power of bottler A presumably bottler B should be free to compete in bottler A's territory.

If the dissent is concerned about the restriction only when it serves to "protect" bottlers with "substantial market power," then it would seem to follow that a bottler without such power might remain protected from intrabrand competition in his territory, since the dissent's per se rule based on market power might not apply to him. He would, however, apparently be free to compete in the territory of a bottler with market power, at least until intrabrand competition dissipates that power. Once the power has been dissipated, the market power per se rule would no longer apply, and the restraint might again be lawful as it would presumably be for similarly situated bottlers who were found not to possess market power. It might then be necessary to monitor each bottler's power periodically to determine when, where, and how long intrabrand competition might be needed to prevent the build-up of "excessive market power."

Thus the dissent reviews the alleged relationship between the restraint, capital formation, and interbrand competition, and is apparently unable to conclude from the record that investments in exclusive territories enhance interbrand competition, are necessary to the continued competitive viability of Coca-Cola and the allied product, or that respondents' capital formation arguments, and the evidence relating to them, justify the restraint. (Dissent at 7). If the burden rests with respondents to establish this defense, as we believe it does[102] the dissent seems to confirm our finding that respondents have not, in this respect, adequately justified their restraint.

The dissent also examines respondents' arguments to the effect that exclusive territories facilitate level pricing by the bottlers and thus "intrabrand competition by enhancing [91] availability." While it is apparently not disputed that market penetration based on level pricing results in price discrimination which "means . . . that some Coca-Cola is provided at less than its actual cost and some is priced above" it is suggested that the cost differentials may not be substantial enough to warrant price differences (Dissent at 9) and that accounting and billing costs may exceed cost differentials or may not justify an expanded price list.[103] Such assumptions, while perhaps a plausible rationale for level pricing in some instances, are largely contrary to evidence cited in this opinion and elsewhere in the dissent. (See Dissent at 14, fn. 27).[104] If prices more accurately reflected actual costs as a result of intrabrand competition, efficient retailers would be in a position to pass any cost savings on to consumers. Under the present system, however, level pricing deprives efficient retailers and their customers of the benefits of such competitive options.[105] Thus the dissent does not seem to resolve the issue of whether respondents have adequately justified the restraint because it aids market penetration by permitting level pricing.

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[100] As we noted previously, it is not possible on this record to state definitively that exclusive territories enhance output to a greater degree than would lower prices resulting from intrabrand competition. (Text at 31, fn. 31, *supra*).

[101] The dissent, while coming close to accepting respondents' arguments that restraint promotes interbrand competition, does not actually do so. (Dissent at 12).

[102] *Sandura, supra; Snap-On Tools, supra; Jim Walter, supra.*

[103] The same analysis might also hold true even if the bottlers have "substantial market power."

The same is true of respondents' advertising and "free-rider" arguments. Judgments concerning the nature of the advertising for Coca-Cola were based on a thorough review of the advertising respondents or bottlers elected to introduce into the record. We certainly do not believe complaint counsel were obligated to provide the evidence upon which a more "systematic and thorough review of Coke advertising" might have been made. (Dissent at 10). Nor do we believe complaint counsel can reasonably be expected to offer evidence showing both the efficiency of the promotional methods respondents now employ and "the relative efficiency of manufacturer (and presumably retailer) advertising versus bottler advertising." (Dissent at 10). [92]

The court in *GTE* was concerned that the *Schwinn* rule declaring exclusive territories per se illegal might result in "a shift to less efficient methods of obtaining the same promotional effects." (*GTE, supra* at 71,901, fn. 25). In applying the rule of reason to these restraints, the court thus opened for further inquiry, on a case-by-case basis, the possibility that promotional methods employed in exclusive territories may be more efficient than alternative promotional methods absent the restraint. The court did not hold, however, that the mere assertion of such efficiency by a respondent without supporting facts was enough to require what the dissent acknowledges to be the "very difficult" process of exploring the "relative efficiency" of alternative methods available in unrestricted markets.

The dissent renders no judgment either about the efficiency of the promotional methods respondents now employ or about the promotional effects they obtain.[106] This is not surprising since respondents did not, in asserting this defense, adduce evidence which would allow such judgments to be made. Consequently, even if complaint counsel had produced evidence of the efficiency of alternative methods of promotion, respondents' failure to establish the efficiency of their own methods would have made, as noted in the dissent, "fine-tuned assessments" of relative efficiency very difficult.

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[104] Yet even if bookkeeping costs justified the continuation of level pricing, the evidence shows that some bottlers are more efficient than others. Thus the level price of some bottlers is likely to be lower or more competitive than the level price charged by others.

[105] With respect to brand availability, the dissent does not contend that if a demand exists for these products at prices which reflect actual costs, the market is unlikely to supply them at competitive prices.

[106] The dissent notes that one such effect might be that the promotion of the Coke brand has conferred substantial market power upon respondents and their bottlers by successfully differentiating their product, but neither this nor any other brand-enhancement effect can be measured based on the evidence in this record. The dissent does not otherwise dispute our analysis which shows that the "free-rider" problem is unlikely to reduce the bottlers' incentives

(Continued)

The dissent's consideration of respondents' quality-control justifications focuses only upon the alleged relationship between territorial restrictions and quality control in distribution.[107] The issue here seems to be whether the [93] Commission may independently evaluate the alleged quality-control justification to determine ". . .whether, assuming some justification for the limitation can be shown, their operation is reasonably related to the needs which brought them into being." *White Motor Co., supra,* 372 U.S. 253, 271 (1973) (Brennan, J. concurring).

According to the dissent, any effort to determine whether the restriction is excessively restrictive "implicitly second-guesses Coke's belief that obstructions to intrabrand competition are needed to maintain the high quality of its product." (Dissent at 12). The situation is the same, though the reverse of the problem considered by the Third Circuit in *American Motor Inns, supra.* In *American Motor Inns,* the court was concerned that plaintiff's lawyers, in a private treble damage action under the Sherman Act, might "conjure up some method of achieving the business purpose in question which would result in a somewhat lesser restriction of trade." Our concern here is in protecting the public interest against the imaginations of entrepreneurs and lawyers who are students of antitrust practice and skillful advocates in defending trade-restrictive conduct. This requires us to assess the competitive effects of respondents' action.[108] The Commission is not bound to accept Coke's belief that obstructions to intrabrand competition are needed when the consequences of its action are excessively trade-restrictive.[109] Further, respondents did not substantiate, and there is really no basis on this record for measuring, the efficiency of territorial restrictions, including, for example, the costs associated with policing and enforcing them, as a quality-control

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to advertise desirable information about price, quality, and services to their customers. (GTE, *supra* at fn. 25; text at 83–34, *supra).*

[107] The relationship between territorial restrictions and quality control in manufacturing is not considered in the dissent.

[108] Certainly no firm is omniscient. The Coca-Cola Co., for example, (1) doubted that carbonated soft drinks could be bottled successfully and sold for home consumption (See Text 10 fn. 12 *supra;* RPF 28) and (2) agreed to sell its syrup at a set price, in perpetuity, without provision for market conditions which might increase the cost of the ingredients used to make the syrup (See *The Coca-Cola Bottling Co.* v. *The Coca-Cola Co. supra).*

[109] *See Coors, supra.* While the combination of price fixing, territorial restrictions, and customer restrictions were found to be per se illegal in *Coors,* the Commission nevertheless fully considered and found merit in some of the quality-control arguments advanced by Coors.

monitoring mechanism. Thus it is unclear whether alternatives, such as an open dating system which might allow the market to monitor product age, would be "less efficient."[110] [94]

Under these circumstances, the language of the Supreme Court in *Northern Pacific Ry.Co.*, noted earlier in this opinion, is appropriate here. The court in that case emphasized that the antitrust laws rest:

> . . . on the premise that the unrestrained interaction of competitive forces will yield the best allocation of our economic resources, the lowest prices, the highest quality and the greatest material progress, while at the same time providing an environment conducive to the preservation of our democratic institutions. But even were that premise open to question, the policy unequivocally laid down by the Act is competition. *Northern Pacific Ry. Co., supra.*

CONCLUSION

Other arguments of the parties, intervenors and amici not specifically addressed in this opinion have been considered and found to be without merit. Having reviewed the record in its entirety, and all of the arguments advanced by respondents in support of these restraints, and having found no adequate justification for the substantial adverse affects these restraints are having on competition in this industry, we conclude that territorial restrictions on the sale of finished Coca-Cola and allied soft drink products are unreasonable restraints on trade, and constitute unfair methods of competition in violation of Section 5 of the Federal Trade Commission Act.

An appropriate order is attached.

FINAL ORDER

This matter having been heard by the Commission upon the appeal of complaint counsel from the initial decision, and upon briefs and oral argument in support thereof and in opposition thereto, and the Commission, for reasons stated in the accompanying opinion, having granted the appeal:

IT IS ORDERED, That the initial decision and order of the administrative law judge be, and they hereby are, vacated, and the findings of fact and conclusions of law contained in the accompanying opinion of the Commission be, and they hereby are, adopted as the findings and conclusions of the Commission in this matter.

Accordingly, the following cease and desist order is hereby entered: [2]

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[110] The dissent invokes what seems to be a "rule-of-plausibility" which would virtually end the evaluation of an alleged justification upon the assertion by a respondent of a plausible link between the restraint and some legitimate business purpose.

ORDER

I

IT IS ORDERED, That the following definitions shall apply in this order:

A. Allied products – the soft drink products of The Coca-Cola Company, other than "Coca-Cola," including Sprite, Fresca, Fanta, Tab and Mr. PiBB, among others;

B. Bottler – any individual, partnership, corporation, association, or other business or legal entity which purchases respondents' syrups or concentrates for use in the manufacture and sale, primarily at wholesale, of finished soft drink beverages;

C. Central warehousing – a method of distribution in which soft drink products are received at a storage facility and either resold or delivered to retail outlets or wholesalers;

D. Concentrate – the basic soft drink ingredients, either dry or liquid, to which sugar is added to prepare a syrup;

E. Confidential commercial information – facts, data, statistics, or other material which concern the business of licensed Coca-Cola or allied product bottlers including, but not limited to, trade secrets, customer lists, plant equipment or production capacities, or syrup and concentrate purchases obtained by or available to, respondents pursuant to, or as a result of, any agreement, understanding, or provision of a trademark license, and which could, if disclosed to a competitor, cause substantial harm to the competitive position of the bottler from whom the material was obtained;

F. Nonrefillable – a special container designed to be filled only once with finished Coca-Cola or allied soft drink beverages;

G. Post-mix syrup – a soft drink ingredient which is used in fountain-dispensing or vending equipment and which is usually sold by bottlers and other wholesalers in steel tanks. A typical post-mix system draws one ounce of syrup from a tank, usually having about a five-gallon capacity, and mixes it at the point of sale with five ounces of carbonated water to produce finished soft drink beverages; [3]

H. Pre-mix system – a system which draws from a tank, usually having about a five-gallon capacity, a finished serving of a soft drink product containing both syrup and carbonated water, "pre-mixed," to produce finished soft drink beverages;

I. Soft drink products – nonalcoholic beverages and colas, carbonated and uncarbonated, flavored and nonflavored, sold in bottles or cans, or through pre-mix or post-mix systems or the like;

J. Syrup – a mixture of ingredients in liquid form which, when mixed with carbonated water, becomes a finished soft drink product.

II

It is further ordered, That The Coca-Cola Company; Coca-Cola Bottling Co. (Thomas), Inc.; Coca-Cola Bottling Works (Thomas), Inc.; and Coca-Cola Bottling Works 3rd, Inc., and the officers, agents, representatives, employees, successors, and assigns of each respondent, directly or through any corporate or other device, in connection with the advertising, merchandising, offering for sale, and sale or distribution of soft drink products, including syrups and concentrates, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from directly or indirectly:

A. Attempting to enter into, entering into, continuing, maintaining, enforcing, or renewing any contract provision, combination, understanding, or agreement to limit, allocate, or restrict the territory in which, or the persons or class of persons to whom, licensed Coca-Cola or allied product bottlers may sell or distribute post-mix syrup or finished soft drink beverages packaged in pre-mix containers or in nonrefillable bottles or cans.

B. Imposing or attempting to impose any limitations or restrictions respecting the territories in which, or the persons or class of persons to whom, bottlers may sell or distribute post-mix syrup or finished soft drink beverages packaged in pre-mix containers or in nonrefillable bottles or cans. [4]

C. Refusing to sell, threatening to refuse to sell, or impairing sales to any bottlers, operating pursuant to a license consented to, granted by, approved by, or ratified by The Coca-Cola Company; Coca-Cola Bottling Co., Inc.; Coca-Cola Bottling Works, Inc.; or Coca-Cola Bottling Works 3rd, Inc., for the duration of the license, anything used in the manufacture and sale of soft drink products, including, but not limited to, syrups and concentrates or the container in which they are sold, or otherwise in any way penalizing any such bottler because of the territory in which, or the persons or class of persons to whom, the bottler sells or distributes post-mix syrup or finished soft drink beverages packaged in pre-mix containers or nonrefillable bottles or cans.

D. Refusing to deliver all of a licensed Coca-Cola or allied product bottler's order for syrups, flavoring, or concentrates because the bottler has made, or intends to make, sales of post-mix syrup or soft drinks packaged in pre-mix containers or nonrefillable bottles or cans to customers outside of the territory granted to the bottler, or because the bottler has made, or intends to make, such sales to customers within the territory granted to the bottler, with knowledge that the customer has transshipped or will transship such soft drinks outside of the territory.

E. Impeding, hindering, or preventing, either directly or indirectly, the methods, including, but not limited to, central warehouse delivery, by which licensed bottlers may distribute Coca-Cola or allied products, *Provided, however*, that respondents may (1) establish quality standards, including standards for the rotation of Coca-Cola and allied products inventories in the central warehouse and at retail delivery locations, irrespective of whether the soft drinks are redelivered from a warehouse or delivered directly to the retail outlet by a bottler; (2) require the bottlers to use a uniform container dating system so that bottlers and retailers will recognize the date without reference to a code; (3) require the bottlers to be responsible, directly or indirectly, for the maintenance of such standards of quality; and (4) require each bottler to place an identification mark of origin on each bottle, bottle cap, or can for the purpose of monitoring compliance with such quality control standards.

F. Enforcing or aiding in the enforcement of any contract provision, agreement, or understanding providing for entry into or examination of the plant and facilities of any independent bottler by another independent bottler. [5]

III

IT IS FURTHER ORDERED, That respondents shall provide for the protection of confidential commercial information acquired from bottler licensees of Coca-Cola or allied product brands as follows:

A. Access to or use of confidential commercial information obtained by respondents, their officers, employees, or agents concerning the production, packaging, distribution, promotion, or sale of Coca-Cola or allied product brands by any licensed bottler shall be restricted to those of respondents' officers, employees, or agents who are neither involved in nor responsible for the production, marketing, promotion, or sale of finished soft drink products by respondents' bottling or canning operations, divisions, subsidiaries, or affiliates.

B. Such officers, employees, or agents who receive, process, or evaluate package-approval requests; process or fill syrup or concentrate purchase orders; conduct on-site inspections of independent bottling plants and facilities; or receive or review confidential commercial information obtained from any independent Coca-Cola or allied product bottler in the course of carrying out the provisions of any soft drink trademark licensing agreement, shall refrain from making any such confidential information available to, or communicating or discussing any such information with, any person involved in or responsible for the production, marketing, promotion, or sale of finished soft drinks by respondents' bottling or canning operations, divisions, subsidiaries, or affiliates.

C. Such officers, employees, or agents who receive, process, or have access to confidential information concerning the business of individual independent Coca-Cola or allied product bottler licensees, shall refrain from suggesting, influencing, or making recommendations to any person concerning the production, distribution, marketing, promotion, or sale of finished soft drinks by respondents' bottling or canning operations, divisions, subsidiaries, or affiliates, *Provided, however*, that this provision shall not apply to respondents' officers, employees, or agents who receive, review, or evaluate data, information, or statistics only in aggregate form or quality control inspection reports which include such information as bacteriological tests, water analyses, water carbonation and syrup content tests, sanitation inspection checks, or bottle washing solution analyses, so long as such reports do not also contain information concerning the bottler's plant equipment, production capacity, or similar types of confidential commercial information. [6]

D. Respondents shall provide each officer, employee, or agent who receives, reviews, or has access to confidential information as set forth in subparagraphs A. through C. above with a copy of this order and an explanation, in writing, of the restrictions this order imposes on access to and the use of such information.

E. Subparagraphs A. through C. above shall not apply (1) to data or information which is in the public domain or which has entered the public domain from a source other than respondents or their officers, employees, or agents; or (2) to transactions involving orders from licensed Coca-Cola or allied product bottlers for finished canned or bottled soft drink products prepared by any respondent for a bottler pursuant to an agency canning or bottling agreement.

IV

IT IS FURTHER ORDERED, That within sixty (60) days from the date The Coca-Cola Company receives service of this order, it shall service a copy of this order upon all bottlers of its soft drink products.

V

IT IS FURTHER ORDERED, That respondents The Coca-Cola Company; Coca-Cola Bottling Co. (Thomas), Inc.; Coca-Cola Bottling Works (Thomas), Inc.; and Coca-Cola Bottling Works 3rd, Inc., shall forthwith distribute a copy of this order to each of their subsidiaries and operating divisions.

VI

It is further ordered, That respondents The Coca-Cola Company; Coca-Cola Bottling Co. (Thomas), Inc.; Coca-Cola Bottling Works (Thomas), Inc.; and Coca-Cola Bottling Works 3rd, Inc., shall notify the Federal Trade Commission at least thirty (30) days prior to any proposed change in the corporate respondents, such as dissolution, assignment, or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any other change which may affect compliance obligations arising out of the order.

It is further ordered, That each respondent shall, within sixty (60) days after service upon it of this order, file with the Commission a report in writing setting forth in detail the manner and form in which it has complied with this order.

Chairman Pertschuk did not participate in the consideration of this matter. Commissioner Clanton dissents.

IN THE MATTER OF

PEPSICO, INC.

ORDER, OPINION, ETC., IN REGARD TO ALLEGED VIOLATION OF SECTION 5 OF THE FEDERAL TRADE COMMISSION ACT

Docket 8856. Complaint, July 15, 1971 — Final Order, April 7, 1978.

This order, among other things, requires a Purchase, N.Y. soft drink manufacturer to cease imposing in any manner territorial limitations or class of customer restrictions on its licensed Pepsi-Cola or allied product bottlers, in connection with the sale or distribution of soft drink products sold in other than refillable containers. The firm is additionally required to provide protection for confidential commercial information submitted by its bottlers.

Appearances

For the Commission: *Raymond L. Hays, Martin A. Rosen, Michael Joel Bloom, Duncan J. Farmer* and *Jeffrey F. Shaw.*

For the respondent: *Milton Handler, Fred A. Freund, Elizabeth Head* and *Richard M. Steuer, Kaye, Scholer, Fierman, Hays & Handler,* New York City. *James G. Frangos* for PepsiCo, Inc., Purchase, N.Y.

For the intervenors: *Robert J. Sisk* and *James B. Kobak, Hughes, Hubbard & Reed,* New York City.

COMPLAINT

The Federal Trade Commission, having reason to believe that PepsiCo, Inc., hereby made and sometimes hereinafter referred to as respondent, or PepsiCo, has violated the provisions of Section 5 of the Federal Trade Commission Act (15 U.S.C. 45), and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. For the purposes of this complaint, the following definitions shall apply:

(a) Bottler – any individual, partnership, corporation, association or other business or legal entity which purchases respondent's concentrate for use in the manufacture and sale, primarily at wholesale, of respondent's pre-mix or post-mix syrups or soft drink products, or who purchases respondent's pre-mix or post-mix syrups or soft drink products for resale, primarily at wholesale;

(b) Central warehousing – a method of distribution in which soft drink products are received at a storage facility and either resold or delivered to retail outlets or wholesalers;

(c) Concentrate – the basic soft drink ingredient sold to bottlers by respondent, which is combined with water and other ingredients for packaging in bottles or cans for sale and distribution as soft drink products, or is used to make post-mix and pre-mix syrups; [2]

(d) Consignment – a form of distribution in which the consignor retains title, dominion, bears all risks of loss and delivers his products to the consignee who is indistinguishable from a salesman or agent;

(e) Place of business – the location of any facilities available to a bottler without regard to customers or geographic area for production or service in the conduct of business operations, to include but not limited to business headquarters, branch sales offices, warehouses and garages, but specifically excluding the plant at which a bottler combines concentrate with water, and possibly other ingredients, for the packaging of soft drink products;

(f) Post-mix syrup – soft drink concentrate which is used in fountain dispensing or vending equipment and is usually sold by bottlers in steel tanks. A typical post-mix system draws one ounce of syrup from a five-gallon tank and mixes it at the point of sale with five ounces of carbonated water to produce 600 six-ounce finished soft drink servings per tank;

(g) Pre-mix syrup – although essentially the same syrup as post-mix, a pre-mix system differs from a post-mix system in that it draws from a five-gallon tank a serving of soft drink products containing both syrup and carbonated water to produce 100 six-ounce finished soft drink servings per tank; and

(h) Soft drink products – nonalcoholic beverages and colas, carbonated and uncarbonated, flavored and nonflavored, sold in bottles and cans, or through pre-mix or post-mix systems or the like.

PAR. 2. Respondent is a corporation organized, existing and conducting its business under and pursuant to the laws of the State of Delaware. It maintains its executive offices and principal place of business at Anderson Hill Road, Purchase, New York. Respondent had sales of $848,265,196 and assets of $471,915,996 in 1969. In 1968, PepsiCo made domestic sales to over 500 bottlers located in every State of the United States.

PAR. 3. Respondent is engaged principally in the manufacture and sale of concentrate which it sells to its over 500 bottlers who purchase the concentrate under a license to produce and sell soft drink products under respondent's trade names such as "Pepsi-Cola," "Diet Pepsi-Cola," "Mountain Dew," "Teem" and "Patio." PepsiCo bottlers combine the concentrate with water and other ingredients and package the mixture in bottles and cans for resale as soft drink products to retailers. In addition to manufacturing and selling concentrate to its bottlers, PepsiCo operates bottling plants in 25 areas of the United States and sells soft drink products to retailers. [3]

PAR. 4. Respondent is engaged in "commerce" within the meaning of the Federal Trade Commission Act (15 U.S.C. 44) in that a continuous flow of interstate commerce in concentrate and soft drink products exists between its headquarters and production facilities and the numerous bottlers located throughout the United States which purchase their products.

PAR. 5. In the course and conduct of its business, respondent, except to the extent limited by the acts, practices and methods of competition hereinafter alleged, has been and is now in competition with other corporations, firms, partnerships and persons engaged in the manufacture, processing, distribution and sale of soft drink products in commerce.

PAR. 6. PepsiCo has hindered, frustrated, lessened and eliminated competition in the distribution and sale of pre-mix and post-mix syrups and soft drink products sold under its trade names by restricting its bottlers from selling outside of a designated geographical area. This restriction is set forth in the agreements between respondent and its bottlers. A typical agreement between respondent and its bottlers provides that the bottler is permitted "to bottle and distribute the carbonated beverage (herein called the 'Beverage'), sold under the trademarks Pepsi and Pepsi-Cola (herein collectively called the 'Beverage trademark'), in the following described territory (herein referred to as the 'Territory'), and nowhere else, bounded as follows: . . ."

PAR. 7. The aforesaid agreements used by respondent have had, and may continue to have, the following effects:

(a) Competition between and among respondent's bottlers in the distribution and sale of "Pepsi-Cola," "Diet Pepsi-Cola," "Mountain Dew," "Teem" and "Patio" brands of soft drink products has been eliminated;

(b) Competition between and among PesiCo's bottling operations and its bottlers in the distribution and sale of PepsiCo soft drink products at the wholesale level has been eliminated;

(c) Innumerable retailers and other customers have been deprived of the right to purchase "Pepsi-Cola," "Diet Pepsi-Cola," "Mountain Dew," "Teem" and "Patio" brands of soft drinks products from the bottler of their choice at a competitive price; and [4]

(d) Consumers of "Pepsi-Cola," "Diet Pepsi-Cola," "Mountain Dew," "Teem" and "Patio" brands of soft drink products have been deprived of the opportunity of obtaining such products in an unrestricted market and at competitive prices.

PAR. 8. Respondent's contracts, agreements, acts, practices and methods of competition aforesaid have had, and may continue to have, the effect of lessening competition in the advertising, merchandising, distribution, offering for sale and sale of pre-mix and post-mix syrups and soft drink products; deprive, and may continue to deprive, the public of the benefits of competition in the purchase of soft drink products; and constitute unfair methods of competition and unfair acts or practices, in commerce, in violation of Section 5 of the Federal Trade Commission Act.

INITIAL DECISION BY JOSEPH P. DUFRESNE, ADMINISTRATIVE LAW JUDGE

OCTOBER 3, 1975

PRELIMINARY STATEMENT

In a complaint dated July 15, 1971, the Commission charged PepsiCo, Inc. with violation of Section 5 of the Federal Trade Commission Act (15 U.S.C. 45). The crux of the charges was that the territorial exclusivity provisions in trademark licensing contracts PepsiCo enters with its [2] bottlers impose an illegal restraint on competition. The provision limits the geographical territory in which a bottler may manufacture and sell Pepsi-Cola products.

It was alleged that the illegal effects of the provision were that competition had been eliminated:

(a) between independent bottlers of PepsiCo products;

(b) at the wholesale level between independent bottlers of PepsiCo products and PepsiCo's own bottlers;

(c) in that retailers and other customers had been deprived of the right to purchase PepsiCo products from the bottler of their choice at a competitive price; and

(d) in that consumers of PepsiCo products had been deprived of the opportunity of obtaining PepsiCo products in an unrestricted market and at competitive prices.

In its answer, PepsiCo admitted that it is engaged in "commerce" within the meaning of the Federal Trade Commission Act (15 U.S.C. 44) (Answer, pp. 4–5).

In summary, as affirmative defenses, PepsiCo stated that:

(a) the bottling appointments are valid exclusive representation agreements creating lawful ancillary restraints which are essential, fair and reasonable and not in violation of Section 5 of the Federal Trade Commission Act (Answer, p. 6);

(b) the complaint was fatally defective because it did not join the bottlers as respondents (Answer, pp. 6–7);

(c) the complaint was barred by laches and the statute of limitation (Answer, p. 7); and

(d) the complaint failed to state a claim upon which relief could be granted (Answer, p. 7). [3]

Because of the time which has elapsed since the complaint issued, it is appropriate to set forth a listing of significant actions by both sides which took place after July 15, 1971. These were:

1. On July 30, 1971, a Motion for Consolidation of this case with Dkts. 8853–8859, which pertain to exclusive territory provisions in the bottler licensing contracts used for other national brands of soft drinks, was filed by complaint counsel. That motion was denied by the administrative law judge on September 28, 1971.

2. On October 12, 1971, a Motion to Dismiss the complaint for nonjoinder of indispensable parties was filed by PepsiCo. The administrative law judge denied the motion on January 20, 1972. The appeal to the Commission was denied on March 23, 1972 (80 F.T.C. 1023). The appeal from that decision to the United States District Court for the Southern District of New York was denied on June 8, 1972 (343 F. Supp. 396). PepsiCo's complaint to the court sought a preliminary injunction to bring a halt to the Commission's proceeding. The court granted the Commission's request that the complaint be dismissed. The Court of Appeals for the Second Circuit affirmed on November 20, 1972 (472 F.2d 179) and the Supreme Court denied certiorari on October 9, 1973 (414 U.S. 876).

3. On November 22, 1971, the petitions of Pepsi-Cola Bottler's Association and of several bottlers of Pepsi-Cola to intervene in the proceedings were granted. As a result, there were three (3) individual bottler intervenors ((1) Pepsi-Cola Albany Bottling Company Inc. (2) Pepsi-Cola Bottling Company of Central Virginia and (3) Pepsi-Cola Bottling Company of Tampa) plus the Association, of which five hundred twelve (512) of the five hundred thirteen (513) of the Pepsi-Cola bottlers are members, who had standing to participate in the proceedings.

4. On July 31, 1972, former complaint counsel filed a motion for partial summary decision. That motion was denied by the administrative law judge on May 3, 1973.

5. On November 28, 1973, counsel for PepsiCo filed a motion to notify or join bottlers and requested that it be certified to the Commission. The motion was certified to the Commission by the administrative law judge on April 1, 1974. The motion was denied by the Commission on May 8, 1974. [4]

6. On January 14, 1974, a motion to discontinue the proceedings and for certification of the motion to the Commission was filed by counsel for PepsiCo. The administrative law judge certified the motion to the Commission on April 1, 1974. The Commission denied the motion on May 14, 1974.

7. Various requests for orders to protect confidential information of PepsiCo and others who supplied such information, were filed and granted during 1974 and 1975.

8. On December 17, 1974, counsel for PepsiCo filed a motion for informative disclosure of complaint counsel's affirmative case. This motion was denied by the administrative law judge on January 22, 1975.

9. On May 19, 1975, a motion to establish matters not at issue was filed by counsel for PepsiCo. The motion was denied by the administrative law judge on May 30, 1975.

10. The litigative hearings began on August 4, 1975, but on August 5, 1975, after several stipulations had been agreed upon and made a part of the record, the parties requested time to negotiate a stipulation which would obviate the need for further evidentiary hearings. Such a stipulation was executed on August 6, 1975. The text follows:

STIPULATION

It is hereby stipulated and agreed by and among respondent, intervenors and complaint counsel in the Matter of PepsiCo, Inc. (Docket No. 8856), subject to the approval of the Administrative Law Judge and the Federal Trade Commission, as follows:

1. All signatories agreed that the purpose of this stipulation is to obviate the need for a separate and lengthy trial record on the merits in PepsiCo, Inc. (Docket No. 8856) because the completed trial record in a companion matter. The Coca-Cola Company, et al. (Docket No. 8855, hereinafter "Coca-Cola proceeding"), is deemed by all signatories as an appropriate basis for an adjudication on the merits in this proceeding. All signatories further agree that use of the trial record of the Coca-Cola proceeding, and [5] all agreements, admissions and waivers in paragraphs 1 through 9 of this Stipulation, shall be for the purpose of this proceeding only and shall have no effect in any other proceeding. As used in this Stipulation, "this proceeding" means Matter of PepsiCo, Inc. (Docket No. 8856) and all appeals, reviews and procedures, both before the Commission and in the federal judiciary system, with respect thereto.

2. Respondent and the intervenors admit all of the jurisdictional facts set forth in the complaint in this proceeding. In the signing of this Stipulation, respondent's answer and all pleadings inconsistent with this admission are deemed to be amended to conform to such admission for the purpose of this proceeding only.

3. Respondent and intervenors agree and admit that the Federal Trade Commission has jurisdiction of this proceeding (Docket No. 8856) and of the respondent and intervenors and that this proceeding is in the public interest.

4. All signatories waive all provisions of the Commission's Rules of Practice and the provisions of all federal statutes including, but not restricted to, the Federal Trade

Commission Act and the Administrative Procedure Act, which are inconsistent with the procedures established in this Stipulation.

5. All signatories agree that they will accept the following actions or determinations by the Administrative Law Judge:

a. The Administrative Law Judge's findings of ultimate facts, conclusions of law and order issued in the Coca-Cola proceeding may be incorporated by reference and made a part of this proceeding by the Administrative Law Judge in whole or to the extent determined by him to be applicable to the [6] acts and practices charged in the Complaint in this proceeding.

b. The Administrative Law Judge may accord respondent's relevant agreements the same construction as accorded to those comparable agreements in the Coca-Cola proceeding.

c. The entire trial record in the Coca-Cola proceeding shall be incorporated by reference and made a part of this proceeding. The Administrative Law Judge may select or designate portions thereof which are or are not applicable in this proceeding as bearing upon the ultimate determination of the legality or illegality of respondent's agreements which he deems to be comparable to those in issue in the Coca-Cola proceeding, and the acts and practices pertinent thereto.

d. As so incorporated in full, and as may be thereafter selected or designated by the Administrative Law Judge, such trial record may have equal force, effect and validity as a full trial record in an adversary hearing before the Administrative Law Judge on the allegations of the Commission's complaint in this proceeding.

e. The ultimate acts, practices and failures to act, with the results and effects thereof, as found by the Administrative Law Judge in his findings and decision in the Coca-Cola proceeding to be the acts or omissions of respondents and intervenors therein may be deemed, in whole or in part, by the Administrative Law Judge to be the ultimate acts, practices and failures to act, with the results and effects thereof, of PepsiCo and intervenors in this proceeding. [7]

f. In issuing his findings of fact, conclusions of law and order in this proceeding, the Administrative Law Judge may make such technical evidentiary amendments and adaptations with respect to the trial record in this proceeding as may be necessary to effect the purposes of this Stipulation.

6. All signatories agree that:

a. If the Administrative Law Judge's findings and conclusions shall be adverse to respondent or intervenors in this proceeding, respondent and intervenors reserve the right to make application to be heard as to the matter of the relief or the form of an order. In the event such an application to be heard is made, any signatory shall have the right to oppose such application, both as to form and substance, and to further contest and challenge the procedures and merits of any proceedings which ensue as a result of the granting of any such application in whole or in part.

b. If the Administrative Law Judge dismisses the complaint in full in the Coca-Cola proceeding, then a like order, founded upon appropriate findings of fact and conclusions of law in this proceeding, shall be deemed by all signatories to be entered herein, subject to the full and complete rights of complaint counsel to appeal and seek review of such order entered in this proceeding.

7. The procedural rights of the signatories with respect to review or appeal to the Commission or any court from any decision, findings of fact, conclusions of law, order or other ruling, which may be entered in this proceeding [8] by the Administrative Law Judge, including the implementation of this Stipulation, shall not be impaired.

8. At the time when the Administrative Law Judge's decision on the merits in this proceeding comes before the Commission for review, or at such other time as the Commission on its own motion may direct, the Commission, acting in the exercise of its

sole discretion and without notice to the signatories, may reject this Stipulation and the procedures adopted thereunder. Any ordered remand to the Administrative Law Judge shall be without prejudice to the signatories.

9. In the event that the Commission elects to confirm this Stipulation and the procedures and action taken pursuant thereto, the procedural rights of respondent and intervenors with respect to review of, or appeal from, any decision or order which the Commission may issue shall not be impaired.

10. It is further stipulated and agreed by and between respondent and intervenors only, and not complaint counsel, that to the extent the restraint which is challenged in this proceeding is upheld, respondent will construe all its Exclusive Bottling Appointments as imposing upon all its bottler trademark licensees thereunder a vertical territorial limitation confining their sales thereunder within the respective territories defined therein and prohibiting direct or indirect sales by them outside such defined territories.

We are proceeding on the basis of the understandings recited in the stipulation because it is apparent that if witnesses had been called to testify at a litigative hearing of this matter, their testimony would have been substantially the same as that of the witnesses who testified in the Coca-Cola hearings. Bottlers of Coca-Cola, Pepsi-Cola, Dr Pepper and of other national brand soft drinks testified in the Coca-Cola [9] hearings and it is clear that the interests and experiences of these bottlers were sufficiently similar to warrant reliance on that testimony in deciding this matter.

11. On August 14, 1975, the testimony of Walter S. Mack, former president of the Pepsi-Cola Company, was taken before me in order to preserve it for possible introduction into the record of this matter in the event the litigative hearings are resumed. Thereafter, the parties agreed to the testimony being added to the limited record of the case.

The findings of fact following are based on a review of the allegations made in the complaint, respondent's answers and the four stipulations entered by counsel which are a part of the evidentiary record of this proceeding. The testimony of Victor A. Bonomo, the current president of PepsiCo, was not considered because he did not finish his direct testimony and was not cross-examined.

In accordance with the stipulation quoted above, certain portions of the initial decision of In the Matter of Coca-Cola Company (Dkt. 8855), a copy of which is appended hereto, have been incorporated in this decision and made applicable to PepsiCo. Reference should be made to that document for a complete understanding of the decision in this proceeding.

For the convenience of the Commission and other readers of this initial decision, the findings of fact include references to supporting evidentiary items in the PepsiCo (Dkt. 8856) and Coca-Cola (Dkt. 8855) records. Such references are intended to serve as guides to the testimony, evidence and exhibits supporting the findings of fact. They do not necessarily represent complete summaries of the evidence considered in arriving at such findings. The following abbreviations have been used:

CX – Commission's Exhibit, followed by number of exhibit being referenced.
RX – Respondent's Exhibit, followed by number of exhibit being referenced.
Tr. – Transcript preceded by the name of the witness and followed by the page number. [10]
Mack Tr. – Transcript of the deposition of Walter S. Mack.

FINDINGS OF FACT

PepsiCo, Inc.

1. PepsiCo, Inc. is a corporation organized, existing and conducting its business under and pursuant to the laws of the State of Delaware. It maintains its executive offices and principal place of business at Anderson Hill Road, Purchase, New York. PepsiCo, Inc. had consolidated sales of $848,265,196 and consolidated assets, including non-soft drink and foreign sales and assets, of $471,915,966 in 1968. In 1968, PepsiCo, Inc. made domestic sales to approximately 500 bottlers in the United States. (Admitted in Answer; Stipulation No. 2, Tr. 285–86)

2. PepsiCo, Inc. is engaged, through its Pepsi-Cola Company division, in the manufacture and sale of concentrates and syrups which it sells to approximately 500 bottlers in the United States who purchase such concentrates or syrups under the terms of exclusive bottling appointment agreements licensing such bottlers to manufacture and sell soft drink products under PepsiCo, Inc.'s trademarks such as "Pepsi-Cola," "Pepsi," "Diet Pepsi-Cola," "Mountain Dew," "Teem," and "Patio." PepsiCo, Inc.'s licensed bottlers manufacture, can and/or bottle and package the soft drink products sold under PepsiCo's trademarks. In addition, subsidiaries of PepsiCo, Inc. operate approximately 20 bottling plants in various parts of the United States and sell the products of such plants. (Admitted in Answer; Stipulation No. 2, Tr. 286)

3. PepsiCo, Inc. has been and is now in competition with others engaged in the manufacture and sale of concentrates, syrups or soft drink products in commerce. (Admitted in Answer)

4. The Pepsi-Cola Company was a relatively late entrant into a soft drink market dominated by The Coca-Cola Company. (Mack. Tr. 82) In 1931, Pepsi-Cola was bankrupt and its assets had been sold by the trustee for $10,500. At the end of 1933, Pepsi-Cola hit upon a successful

marketing strategy — sale of Pepsi in 12-ounce [11] bottles for the same 5¢ price charged for 6 1/2-ounce bottles of Coca-Cola and a vigorous drive to recruit independent franchisees. (Stipulation No. 3, Tr. 295)

5. In 1932 and 1933, Pepsi-Cola had been bottled for the Pepsi-Cola Company and was sold principally in the New York metropolitan area. Arrangements were made for bottling Pepsi-Cola in a few other cities in 1934. But by the end of 1934, it became apparent that Pepsi-Cola's new found success with its "twice as much for a nickel" strategy could become permanent only if it were possible to build a large nationwide sales volume quickly. Pepsi-Cola Company, with its limited resources and distribution facilities, could not itself capitalize on the impact of its 12-ounce drink. (Mack, Tr. 15) Franchising local independent businessmen to bottle Pepsi provided a solution to the problem. (Stipulation No. 3, Tr. 295–96)

6. By promising exclusive territorial rights, which granted to the licensee,. among other rights, the exclusive right to manufacture, distribute and sell trademarked soft drink products in a defined geographical area, Pepsi-Cola representatives were able to persuade local bottlers across the country to become Pepsi-Cola franchisees. (Stipulation No. 3, Tr. 296; Mack, Tr. 13, 16)

7. The emergence of Pepsi as a nationally recognized cola drink depended on the network of independent bottler appointments issued in the mid-1930's. The franchise system was the cornerstone of Pepsi-Cola's steady campaign to become a viable, aggressive competitor to Coca-Cola. The effectiveness of this campaign was in turn dependent on the determination, business acumen and financial stability of Pepsi-Cola's franchisees. In order to induce individuals with the requisite financial and managerial resources to establish a local bottling plant, effectively exploit market potential and win consumer approval of its relatively unknown cola drink, the Pepsi-Cola Company had to demonstrate its commitment to the franchisee's success. (Stipulation No. 3, Tr. 297)

8. This it did by granting the bottlers the exclusive right to bottle and sell Pepsi in their designated franchise areas. Appointment as a Pepsi-Cola franchisee meant that the local bottler must make a substantial capital investment in plant, bottling machinery, bottles, cases, trucks, [12] equipment and supplies. He had to be willing to devote substantial personal and financial resources on behalf of a relatively unknown drink, the ultimate acceptance of which in the national market was far from certain, and to battle Coca-Cola which had been even further entrenched by the recent bankruptcy of the predecessor Pepsi-Cola Company. Without exclusive territorial fran-

chises Pepsi-Cola Company would have been unable to achieve the nationwide sales volume essential to enable it to compete successfully with Coca-Cola. (Stipulation No. 3, Tr. 297; Mack, Tr. 11–13, 16–16A, 29)

9. The domestic Pepsi-Cola bottling appointment agreements of PepsiCo, Inc. provide that the bottler is appointed as PepsiCo, Inc.'s "exclusive bottler, to bottle and distribute the carbonated beverage (herein called the 'Beverage'), sold under the trademarks Pepsi and Pepsi-Cola (herein collectively called the 'Beverage trademark'), in the following described territory (herein referred to as the 'Territory'), and nowhere else, bounded as follows: . . ." and refers to said agreement for the complete terms thereof. (Stipulation No. 2, Tr. 287)

10. As part of the effort to establish Pepsi as a nationally accepted cola drink, eight wholly-owned subsidiaries of Pepsi-Cola Company were formed during the period 1931–1937 for the purpose of operating Pepsi-Cola franchises in their states of incorporation. Some of these franchises were later granted to local businessmen, while franchises for the New York, Newark, Pittsburgh, Philadelphia, and Boston metropolitan areas were retained. They served to insure the presence of Pepsi-Cola in these important markets, to promote consumer acceptance in those markets, and contributed to the goal of making the product available everywhere. (Stipulation No. 3, Tr. 298)

11. Following World War II, the ratio of Pepsi sales to sales of Coca-Cola began an upward climb; and by the mid-1950's the latter's commanding lead in bottle sales of 5 to 1 over Pepsi in 1940 had been reduced to 2.5 to 1. By 1960, Pepsi had become a strong contender to Coca-Cola, having further reduced its lead in the total market to 2 to 1 and in food stores, where consumers can pick and choose freely between competing brands, Pepsi was outsold by Coca-Cola only 1.2 to 1. (Stipulation No. 3, Tr. 298–99) [13]

Interstate Commerce

12. PepsiCo, Inc. is engaged in "commerce" within the meaning of the Federal Trade Commission Act (15 U.S.C. 44). (Admitted in Answer; Stipulation No. 2, Tr. 286)

The Soft Drink Industry and the Exclusive Territorial Franchise System

13. In accordance with the stipulation of the parties (see pp. 4–8, *supra*), the following findings of fact from the initial decision of *In the Matter of The Coca-Cola Company* (Dkt. 8855) are deemed applicable to respondent in this proceeding and are incorporated by reference

herein: Nos. 27–55, 58–59, 63–70, 72–122, 124–127, 129–149, 151–195 (pp. 15–24, 25, 28–29, 29–50, 50–52, 53–60, 60–76). Where the words "Coca-Cola" (the company) and Coca-Cola (the drink) appear, they should be read, as appropriate, PepsiCo and Pepsi-Cola.

DISCUSSION AND CONCLUSIONS OF LAW

In accordance with the stipulation of the parties (see pp. 4–8, *supra*), the discussion of the applicable legal principles and the conclusions of law from the initial decision of *In the Matter of The Coca-Cola Company* (Dkt. 8855) are incorporated by reference herein.

ORDER

It is ordered, That the complaint in this matter be, and it hereby is, dismissed.

DISSENTING STATEMENT OF COMMISSIONER CLANTON

For the reasons expressed in my dissenting statement in the companion case involving the Coca-Cola Company, Dkt. 8855, I dissent from the Commission's decision with respect to PepsiCo, Inc.

OPINION

BY DOLE, *Commissioner:*

The complaint in this matter charges PepsiCo, Inc., with imposing territorial restrictions on the sale of Pepsi-Cola and allied products produced by independent bottlers, in violation of Section 5 of the Federal Trade Commission Act.

In 1968 PepsiCo had consolidated sales of $848,265,196 and consolidated assets, including non-soft drink and foreign sales and assets, of $471,915,966. Respondent's Pepsi-Cola Company division manufactures and sells soft drink concentrates and syrups to approximately 500 bottlers in the United States under the terms of exclusive bottling appointment agreements which authorize the bottlers to manufacture and sell soft drink products under PepsiCo trademarks, including "Pepsi-Cola," "Mountain Dew," "Teem," and "Patio." In addition to independent Pepsi-Cola and allied product bottlers, subsidiaries of PepsiCo operate approximately 20 bottling plants in various parts of the United States. (Admitted in Answer; Stipulation 2, Tr. 286).

I. STIPULATION OF FACTS

The trial of this case before the judge commenced shortly after the conclusion of the trial involving similar charges alleged in the complaint against *The Coca-Cola Company, et al.*, Dkt. 8855. Following two [2] days of hearings, the parties and intervenors stipulated, *inter alia*, that:

> . . . the completed trial record in a companion matter, The Coca-Cola Co., *et al.*, (Docket No. 8855, hereinafter "Coca-Cola proceeding"), is deemed by all signatories as an appropriate basis for an adjudication on the merits of this proceeding.

The stipulation further provides that, "The entire trial record in the Coca-Cola proceeding shall be incorporated by reference and made part of this proceeding." As so incorporated:

> . . . such trial record may have equal force, effect and validity as a full trial record in an adversary hearing before the Administrative Law Judge on the allegation of the Commission's complaint in this proceeding. (Stipulation ¶5d).

Shortly after this stipulation was entered into the record, the testimony of Walter S. Mack, former President of PepsiCo, was taken before the judge in order to preserve it for possible introduction into the record in the event further litigation became necessary. Thereafter, the judge ordered that Mr. Mack's testimony be added to the record, along with certain exhibits which were offered and received with Mr. Mack's testimony. (Order Placing the Deposition of Walter S. Mack in the Record, entered September 4, 1975, Docket Binder 8856–1–3–2; Supplemental Order to Order of September 4, 1975, entered September 9, 1975). The judge further ordered, pursuant to the stipulation of the parties and intervenors, that the trial record in the Coca-Cola proceedings be incorporated into, and made a part of, the record of this proceeding. The case is now before us on appeal by complaint counsel from an initial decision of the judge dismissing the complaint. The oral arguments of counsel in this matter and in the matter of *The Coca-Cola Company, et al.*, Dkt. 8855, were received at a consolidated hearing on appeal.

The Commission, having reviewed the record in its entirety, has determined that the order entered by the judge dismissing the complaint be vacated. The Commission has further determined that certain findings and conclusions in the opinion of the Commission in the matter of *The Coca-Cola Company, et al.*, Dkt. 8855, as hereinafter noted, shall be adopted as the findings and conclusions [3] of the Commission in this case. In addition, the findings of fact as set forth in the judge's initial decision shall be adopted by the Commission to the extent that they are not inconsistent with the findings and conclusions stated in this opinion.

II. History of PepsiCo and the Restraint

The record shows that the Pepsi-Cola Company had a difficult period of entry into the soft drink market. In 1931 Pepsi-Cola was bankrupt; a trustee sold its assets for $10,500. By 1934, however, the tide began to turn in its favor. It employed a new marketing strategy pursuant to which it sold Pepsi-Cola in 12-ounce bottles for the same price then being charged for 6 1/2-ounce bottles of Coca-Cola.

Prior to 1935, Pepsi-Cola was sold principally in the New York metropolitan area and a few other cities. Despite the success of its "twice as much for a nickel" strategy, respondent lacked the resources and distribution facilities to capitalize on the impact of its 12-ounce drink. (Mack, Tr. 15). Thus it initiated a drive to recruit independent entrepreneurs to bottle its product. (Stipulation No. 3, Tr. 295-96).

As an inducement to attract and encourage individual investors to establish local bottling plants, respondent granted them the exclusive right to bottle and sell "Pepsi" in designated geographic areas. Consequently, the bottling agreements provide that each bottler is appointed as PepsiCo's:

> . . . exclusive bottler, to bottle and distribute the carbonated beverage (herein called the "Beverage"), sold under the trademarks Pepsi and Pepsi-Cola (herein collectively called the "Beverage trademark"), in the following described territory (herein referred to as the "Territory"), and nowhere else, bounded as follows:. . . ." (Stipulation No. 2, Tr. 287; *See also* RX 99, incorporated exhibit from Dkt. 8855).

It is undisputed that a network of independent bottlers was an important part of respondent's plan 40 years ago to expand the sales of Pepsi-Cola in competition nationwide with the bottlers of Coca-Cola. (Stipulation No. 3; Tr. 297, Mack, Tr. 11-13, 16-16A, 29). In addition to the recruitment of independent bottlers, respondent established, [4] during the period of 1931-1937, eight wholly-owned bottling subsidiaries. While some of these franchises were later granted to local businessmen, respondent retained the franchises for the New York, Newark, Pittsburgh, Philadelphia, and Boston metropolitan areas. (Stipulation No. 3, Tr. 298).

Following World War II, the ratio of Pepsi sales to sales of Coca-Cola began an upward climb: in 1940 Coca-Cola's lead in bottle sales was 5 to 1 over Pepsi; by the mid-1950's the lead was 2.5 to 1; by 1960 it was 2 to 1. (Stipulation No. 3, Tr. 298-99). The record further shows that by 1971 Pepsi-Cola had overtaken Coca-Cola as the leading brand in numerous cities (RX 2Y-Z39 incorporated exhibits from Dkt. 8855) and in several regions of the country. (RX 2Y-Z39-40, incorporated exhibits from Dkt. 8855). Thus, while territorial restrictions may have assisted a faltering new entrant into the market four decades ago, those same restrictions certainly cannot be justified as necessary on that basis today.

Respondent PepsiCo is a well-established, dominant soft drink syrup and concentrate producer; its bottlers are firmly entrenched in the fabric of the bottling industry; and PepsiCo brands are established, widely recognized soft drink beverages. Thus the evidence introduced into the record leads us to conclude that these brands could continue to be a viable interbrand competitive force in the market if the bottlers who now sell them are permitted to compete interbrand among themselves.

III. CONTINUING USE OF THE RESTRICTIONS

As we noted previously, the contract between PepsiCo and each of its bottlers provide, and bottlers understand their contracts to mean, that each bottler may sell Pepsi-Cola and allied products exclusively within the territory described in his license agreement and nowhere else.[1] (Mack, Tr. 16–A; *See also* incorporated testimony Dkt. 8855, Tr. 2859, 2861, 2918–20; 2958, 2993; 3108–09). It is arguable that the mere existence of such a provision in a contract between PepsiCo and Pepsi-Cola bottlers constitutes a threat to competition. Pepsi's syrups, concentrates and trademarks are vital to [5] the business of its bottlers, and there is always some danger that PepsiCo will seek to enforce the agreement or that the bottlers, as the record shows, will feel obliged to adhere to it.[2] Yet we need not rely solely upon the mere existence of these agreements; there is evidence in the record of PepsiCo's resolve to enforce compliance with the restriction.

According to respondent's former President, PepsiCo, "would protect their [the bottlers] franchise . . . and do everything we could to protect both the trademark and the name and their territory for them on an exclusive basis." (Mack, Tr. 17; *see also* Mack, Tr. 19, 38, 83, 91–94, 96).

Mr. Mack testified further:

> Q. . . .were there sometimes complaints received by the Pepsi-Cola Company from bottlers that Pepsi-Cola product produced by another bottler was crossing into the complaining bottler's territory?
>
> A. We had very little of that. The bottlers knew that the value of the Pepsi-Cola franchise was his exclusive in this area. And where those things happened inadvertently a letter or one bottler talking to another straightened it out. We had very little of that. The bottlers were a good group. They helped each other.

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[1] Unlike The Coca-Cola Co., respondent PepsiCo also imposes territorial restrictions on the sale of its fountain syrup. (Mack, Tr. 34, 35, 87–89). Whether the restraint is also applicable to the sale and distribution of post-mix systems by Pepsi-Cola bottlers is unclear on this record. The order, however, will cover both post-mix syrup and premix systems as a prophylactic measure. (*See*, Opinion in Dkt. 8855, at 64).

[2] *Accord, Chock Full O' Nuts Corp., Inc.*, 83 F.T.C. 575, 635 (1973).

Q. And they understood and knew the value of the exclusive franchise?

A. Right.

Q. And in those few instances you have described where a letter was written, that was a letter from the Pepsi-Cola Company to the offending bottler?

A. I don't remember ever having to write a letter. The field man usually would talk to him. And if there was an infraction, it was very easily straightened out. We had very little of that sort of trouble. [6]

Q. The field man would be a Pepsi-Cola employee who would talk to the offending bottler and it would be straightened out?

A. Yes. If there was any. We had no problems along that line. (Mack, Tr. 28–29).

The record also shows that respondent's concern for preserving the integrity of its territorial policy was a key consideration in its decision to abandon an innovative Pepsi-Cola canning experiment. The concern arose when a retailer was found transshipping the canned product from its central warehouse to its retail outlets located within the territories of various Pepsi-Cola bottlers.

Thus Mr. Mack testified:

Q. In the post-World War II period did you at some point enter into an experiment in the selling of Pepsi-Cola in cans?

A. Yes.

Q. Would you tell Judge Dufresne about that experiment?

A. It seems to me that we ought to test and find out how it fitted in the picture. So I started an experiment with Pepsi-Cola in cans. It was difficult to get a can that had the lining . . . the ingredients didn't affect (and which did not) . . . affect the flavor by the lining, by the metal. And finally Continental Can worked out a can for me that had a crown top . . . And I started an experiment in three areas because I wanted to test the different consumers.

* * * * * * *

The parent company did the manufacturing. The parent company did the canning. And we shipped it to those three test areas.

Q. What were the results of the test?

A. Well, they were good and they were bad. The good part of it is that we found that the consumer was interested in it. The bad part of it was that it was an expensive operation. And that in some instances it couldn't be confined to the territory that the bottler was in. And we finally withdrew it and took [7] it off the market. We found it wouldn't go with the franchise system.

Q. Will you tell us specifically what the instances were in which you received reports of cans crossing franchise lines?

MR. FREUND: Objection. I don't know that he said he received reports.

JUDGE DUFRESNE: Before you ask that, what did you mean when you said you had problems confining the cans, Mr. Mack?

THE WITNESS: Well, I meant by that that in some instances due to the fact that they didn't have to go back to pick up the empties, they crossed territorial lines.

JUDGE DUFRESNE: You mean the licensee would sell canned product outside of the territory you had agreed upon he would serve, or what?

THE WITNESS: No I mean by that, specifically what happened particularly in the New Rochelle area was that the New Rochelle bottler sold to A&P.

JUDGE DUFRESNE: They might ship it outside?

THE WITNESS: That is right. They had a distribution system in which they went and distributed the way they do Campbells Soup or Heinz Beans or something to their chain stores. And their chain stores might get from a warehouse and be outside the franchise area and therefore cans in New Rochelle might get up into Stanford, Connecticut.

JUDGE DUFRESNE: This was an action by the reseller rather than the Pepsi-Cola?

THE WITNESS: Oh, yes. The bottler didn't do it. It was the reseller. The retailer did that.

JUDGE DUFRESNE: All right. [8]

By Mr. Sisk:

Q. Did the Pepsi-Cola Company receive complaints from the bottlers adjoining the New Rochelle franchise?

A. Yes, we got some complaints, and we withdrew the whole operation.

Q. That was the end of the canning operation as far as you were concerned?

A. Yes. (Mack, Tr. 24-28).

Pepsi-Cola is available today, of course, in both cans and bottles, but the extra-territorial sale or trans-shipment of it is still restricted. The bottlers testified that they do not engage in such sales or shipments, and if they did, it would constitute a breach of the territorial provisions of their bottling appointment agreements. (Testimony of Pepsi-Cola bottlers, Dkt. 8855, Tr. 2875-76, 2992-93, 3108-09).

Consequently, the evidence is uncontroverted that PepsiCo has imposed, by contract, and enforced, in practice, geographic exclusivity, using such methods as may have been necessary to preserve the territorial restrictions challenged in this proceeding. (Mack, Tr. 16, 16-A, 17, 28-29). The evidence further shows that it will, absent an order, continue to do so in the future. (Stipulation ¶10, Tr. 437-38).

IV. EFFECTS OF THE RESTRICTIONS

In accordance with the stipulation of the parties and intervenors, the following findings and conclusions set forth in the text of our opinion in the matter of *The Coca-Cola Company, et al.*, Dkt. 8855, are hereby adopted by the Commission and incorporated herein by reference: Section II through Section III, subsection B (Text at 6-19); Section III, subsection B2 through Section VI, subsection B4 (Text at 21-78); Section VI, subsection B5c and Conclusion (Text at 83-84). Our discussion of the anticompetitive effects of the territorial restriction imposed by The Coca-Cola Company, in the above noted portions of our opinion in Dkt. 8855, is equally applicable here. [9]

In addition, we note that, as a dual-distributing trademark licensor, PepsiCo, like The Coca-Cola Company, has access to competitively sensitive commercial information about each of its bottler's business operations. (*See* RX 99B; Tr. 3102 incorporated from Dkt. 8855).

Therefore, we adopt and hereby incorporate by reference Section VI, subsections 5 and 5a of our Opinion in The *Coca-Cola* case, Dkt. 8855. (Text at 79–81). Section III of our order will provide ancillary safeguards which will prevent PepsiCo from exploiting such information to the detriment of the independent Pepsi-Cola or allied product bottlers.

Respondent and intervenors have reserved the right to be heard as to matters of relief or the form of an order, and they have been afforded the opportunity to be heard on these issues before the Commission. Neither has suggested, however, that relief entered here should be different from the relief in the *Coca-Cola* Case. No distinctions of any significance pertinent to the issues of relief, either with respect to the factual context in which the restraint is imposed by PepsiCo upon its bottlers or with respect to the potential impact lifting the restriction might have upon Pepsi-Cola bottlers, have been brought to our attention. The record supports uniform relief in these companion cases. Accordingly,

An appropriate order is attached.

FINAL ORDER

This matter having been heard by the Commission upon the appeal of complaint counsel from the initial decision, and upon briefs and oral argument in support thereof and in opposition thereto, and the Commission, for reasons stated in the accompanying opinion, having granted the appeal:

It is ordered, That the entire record in the matter of *The Coca-Cola Company, et al.,* Dkt. 8855; be, and it hereby is, incorporated into, and made part of, the record in this proceeding.

It is further ordered, That the findings of fact set forth in the initial decision of the administrative law judge be, and they are, adopted by the Commission to the extent they are consistent with the findings of fact and conclusions of law contained in the accompanying opinion of the Commission in this matter.

It is further ordered, That the order dismissing the complaint entered by the administrative law judge be, and it hereby is, vacated.

Accordingly, the following cease and desist order is hereby entered:

[2]

ORDER

I

It is ordered, That the following definitions shall apply in this order:

A. Allied products – the soft drink products of PepsiCo, Inc., other than "Pepsi-Cola" including "Teem," "Mountain Dew," and "Patio," among others;

B. Bottler – any individual, partnership, corporation, association, or other business or legal entity which purchases respondents' syrups or concentrates for use in the manufacture and sale, primarily at wholesale, of finished soft drink beverages;

C. Central warehousing – a method of distribution in which soft drink products are received at a storage facility and either resold or delivered to retail outlets or wholesalers;

D. Concentrate – the basic soft drink ingredients, either dry or liquid, to which sugar is added to prepare a syrup;

E. Confidential commercial information – facts, data, statistics, or other material which concern the business of licensed Pepsi-Cola or allied product bottlers including, but not limited to, trade secrets, customer lists, plant equipment or production capacities, or syrup and concentrate purchases obtained by or available to, respondent pursuant to, or as a result of, any agreement, understanding, or provision of a trademark license, and which could, if disclosed to a competitor, cause substantial harm to the competitive position of the bottler from whom the material was obtained;

F. Nonrefillable – a special container designed to be filled only once with finished Pepsi-Cola or allied soft drink beverages;

G. Post-mix syrup – a soft drink ingredient which is used in fountain-dispensing or vending equipment and which is usually sold by bottlers and other wholesalers in steel tanks. A typical post-mix system draws one ounce of syrup from a tank, usually having about a five-gallon capacity, and mixes it at the point of sale with five ounces of carbonated water to produce finished soft drink beverages; [3]

H. Pre-mix system – a system which draws from a tank, usually having about a five-gallon capacity, a finished serving of a soft drink product containing both syrup and carbonated water, "pre-mixed," to produce finished soft drink beverages;

I. Soft drink products – nonalcoholic beverages and colas, carbonated and uncarbonated, flavored and nonflavored, sold in bottles or cans, or through pre-mix or post-mix systems or the like;

J. Syrup – a mixture of ingredients in liquid form which, when mixed with carbonated water, becomes a finished soft drink product.

II

It is further ordered, That respondent PepsiCo, Inc., and the officers, agents, representatives, employees, successors, and assigns of respondent, directly or through any corporate or other device, in connection with the advertising, merchandising, offering for sale, and sale or distribution of soft drink products, including syrups and concentrates, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from directly or indirectly:

A. Attempting to enter into, entering into, continuing, maintaining, enforcing, or renewing any contract provision, combination, understanding, or agreement to limit, allocate, or restrict the territory in which, or the persons or class of persons to whom, licensed Pepsi-Cola or allied product bottlers may sell or distribute post-mix syrup or finished soft drink beverages packaged in pre-mix containers or in nonrefillable bottles or cans.

B. Imposing or attempting to impose any limitations or restrictions respecting the territories in which, or the persons or class of persons to whom, bottlers may sell or distribute post-mix syrup or finished soft drink beverages packaged in pre-mix containers or in nonrefillable bottles or cans. [4]

C. Refusing to sell, threatening to refuse to sell, or impairing sales to any bottlers, operating pursuant to a license consented to, granted by, approved by, or ratified by PepsiCo, Inc., for the duration of the license, anything used in the manufacture and sale of soft drink products, including, but not limited to, syrups and concentrates or the container in which they are sold, or otherwise in any way penalizing any such bottler because of the territory in which, or the persons or class of persons to whom, the bottler sells or distributes post-mix syrup or finished soft drink beverages packaged in pre-mix containers or nonrefillable bottles or cans.

D. Refusing to deliver all of a licensed Pepsi-Cola or allied product bottler's order for syrups, flavoring, or concentrates because the bottler has made, or intends to make, sales of post-mix syrup or soft drinks packaged in pre-mix containers or nonrefillable bottles or cans to customers outside of the territory granted to the bottler, or because the bottler has made, or intends to make, such sales to customers within the territory granted to the bottler, with knowledge that the customer has transshipped or will transship such soft drinks outside of the territory.

E. Impeding, hindering, or preventing, either directly or indirectly, the methods, including, but not limited to central warehousing, by which licensed bottlers may distribute Pepsi-Cola or allied products, *Provided, however,* that responsdent may (1) establish quality standards, including standards for the rotation of Pepsi-Cola and allied product inventories in the central warehouse and at retail delivery locations, irrespective of whether the soft drinks are redelivered from a warehouse or delivered directly to the retail outlet by a bottler; (2)

require the bottlers to use a uniform container dating system so that bottlers and retailers will recognize the date without reference to a code; (3) require the bottlers to be responsible, directly or indirectly, for the maintenance of such standards of quality; and (4) require each bottler to place an identification mark of origin on each bottle, bottle cap, or can for the purpose of monitoring compliance with such quality control standards.

F. Enforcing or aiding in the enforcement of any contract provision, agreement, or understanding providing for entry into or examination of the plant and facilities of any independent bottler by another independent bottler. [5]

III

It is further ordered, That respondent shall provide for the protection of confidential commercial information acquired from bottler licensees of Pepsi-Cola or allied product brands as follows:

A. Access to or use of confidential commercial information obtained by respondent, its officers, employees, or agents concerning the production, packaging, distribution, promotion, or sale of Pepsi-Cola or allied product brands by any licensed bottler shall be restricted to those of respondent's officers, employees, or agents who are neither involved in nor responsible for the production, marketing, promotion, or sale of finished soft drink products by respondent's bottling or canning operations, divisions, subsidiaries, or affiliates.

B. Such officers, employees, or agents who receive, process, or evaluate package-approval requests; process or fill syrup or concentrate purchase orders; conduct on-site inspections of independent bottling plants and facilities; or receive or review confidential commercial information obtained from any independent Pepsi-Cola or allied product bottler in the course of carrying out the provisions of any soft drink trademark licensing agreement, shall refrain from making any such confidential information available to, or communicating or discussing any such information with, any person involved in or responsible for the production, marketing, promotion, or sale of finished soft drinks by respondent's bottling or canning operations, divisions, subsidiaries, or affiliates.

C. Such officers, employees, or agents who receive, process, or have access to confidential information concerning the business of individual independent Pepsi-Cola or allied product bottler licensees, shall refrain from suggesting, influencing, or making recommendations to any person concerning the production, distribution, marketing, promotion, or sale of finished soft drinks by respondent's bottling or canning operations, divisions, subsidiaries, or affiliates, *Provided, however*, that this provision shall not apply to respondent's officers, employees, or agents who receive, review, or evaluate data, information, or statistics only in aggregate form or quality control inspection reports which include such information as bacteriological tests, water analyses, water carbonation and syrup content tests, sanitation inspection checks, or bottle washing solution analyses, so long as such reports do not also contain information concerning the bottler's plant equipment, production capacity, or similar types of confidential commercial information. [6]

D. Respondent shall provide each officer, employee, or agent who receives, reviews, or has access to confidential information as set forth in subparagraphs A. through C. above with a copy of this order and an explanation, in writing, of the restrictions this order imposes on access to and the use of such information.

E. Subparagraphs A. through C. above shall not apply (1) to data or information which is in the public domain or which has entered the public domain from a source other than respondent or its officers, employees, or agents; or (2) to transactions involving orders from licensed Pepsi-Cola or allied product bottlers for finished canned or bottled soft drink products prepared by respondent for a bottler pursuant to an agency canning or bottling agreement.

IV

It is further ordered, That within sixty (60) days from the date respondent receives service of this order, it shall service a copy of this order upon all bottlers of its soft drink products.

V

It is further ordered, That respondent shall forthwith distribute a copy of this order to each of its subsidiaries and operating divisions.

VI

It is further ordered, That respondent shall notify the Federal Trade Commission at least thirty (30) days prior to any proposed change in the corporate respondent, such as dissolution, assignment, or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any other change which may affect compliance obligations arising out of the order.

It is further ordered, That respondent shall, within sixty (60) days after service upon it of this order, file with the Commission a report in writing setting forth in detail the manner and form in which it has complied with this order.

Chairman Pertschuk did not participate in the consideration of this matter. Commissioner Clanton dissents.

IN THE MATTER OF

HOWARD ENTERPRISES, INC.

Docket 9096. Interlocutory Order, April 7, 1978

Order directing that oral argument not be set down without a further order of the Commission.

ORDER GRANTING MOTION TO OMIT ORAL ARGUMENT

On March 13, 1978, complaint counsel filed with the Secretary a motion dated March 8 to omit oral argument pursuant to Rule Section 3.52(f). The grounds urged for the motion were that the case presented essentially legal issues and that these were fully discussed in complaint counsel's brief. Counsel for the respondents, contacted telephonically by the Secretary, declined to oppose the motion.

That the issues presented by a case are legal rather than factual bears no necessary relationship to the value of oral argument, which serves as an opportunity to sharpen and define the opposing positions of the parties, and to probe the implications of their arguments, whatever the nature of the issues. However, we will defer provisionally to the evident judgment of both counsel that the issues here will be fully elaborated in the briefs. If the Commission should determine, once all the briefs are available, that oral argument would nonetheless be useful, it can so order at that time.

Accordingly, *it is ordered*, That no date for oral argument in this matter shall be set down without a further order of the Commission.

IN THE MATTER OF

KELLOGG COMPANY, ET AL.

Docket 8883. Interlocutory Order, April 19, 1978

Denial of Kellogg's applications (1) for review of ALJ's order denying motion to nullify subpoenas duces tecum for taking of depositions and production of documents, and (2) for stay of deposition program pending resolution of application for review.

ORDER DENYING APPLICATIONS OF KELLOGG COMPANY FOR REVIEW AND FOR A STAY

On April 13, 1978, respondent Kellogg Company ("Kellogg"), filed with the Commission an Application for Review of Order Denying Its Motion to Nullify Subpoenas Duces Tecum for the Taking of Depositions and Production of Documents. With that Application, Kellogg also filed an Application for a Stay of the Commencement of Complaint Counsel's Deposition Program Pending Resolution of Kellogg Company's Application for Review. For the reasons briefly outlined below, the Commission denies both Applications.

Kellogg's Application for Review comes to the Commission without the certification of the Administrative Law Judge pursuant to Commission Rule 3.23(b). Under the Commission's Rules, that certification is essential for interlocutory review unless the matter is one which falls within the provisions of Rule 3.23(a). Kellogg cites to Reorganization Plan No. 4 of 1961, H. Doc. No. 159, 87th Cong., 1st Sess., as support for its appeal without certification. Even that Plan, however, provides that the Commission shall retain its discretionary right to review "within such time and in such manner as the Commission shall by rule prescribe . . . ." In this instance, the Commission has explicitly provided for review under Rule 3.23(b) or after issuance of the Administrative Law Judge's initial decision.

The Commission's Rules are designed to provide for the orderly and efficient conduct of a hearing. That process would be seriously undercut if the Commission were to interject itself into every dispute between the parties and the law judge. Interlocutory review is the exception to the rule that the Administrative Law Judge is vested with broad discretionary powers to conduct the proceeding. Rule 3.42(c).[1] In fact, this is precisely the kind of matter which is peculiarly within the province of the Administrative Law Judge as the trier of fact. Accordingly,

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[1] As we have noted on other occasions, *Kellogg Co., et al.*, 83 F.T.C. 1756 (1974); *Warner-Lambert Co.*, 83 F.T.C. 485 (1973), there may be instances where review is appropriate even without certification upon showing of a clear abuse of discretion by the Administrative Law Judge, and prejudice to the appealing party. That is certainly not the case here.

It is ordered, That the Application of Kellogg Company for Review of Order Denying Its Motion to Nullify Subpoenas Duces Tecum for the Taking of Depositions and Production of Documents, and the Application of Kellogg Company for a Stay of the Commencement of Complaint Counsel's Deposition Program Pending Resolution of Kellogg Company's Application for Review be, and the same hereby is, denied.

IN THE MATTER OF

INSILCO CORPORATION, ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATIONS OF THE FEDERAL TRADE COMMISSION AND TRUTH IN LENDING ACTS

Docket C-2919. Complaint, April 19, 1978 — Decision, April 19, 1978

Consent order requiring a Meriden, Conn., distributor of pre-cut housing products and its subsidiary, among other things, to cease misrepresenting or failing to make relevant disclosures with regard to product assembly, delivery costs, legal building requirements, need for skilled building tradesmen, mortgage liens, and cancellation rights–in Spanish, if applicable. The order further requires the firm to acknowledge and resolve complaints in a prescribed manner. Additionally, the firm must cease failing to provide consumers, in connection with the extension of credit, such material disclosures as required by Federal Reserve Board regulations.

Appearances

For the Commission: *Blanche Stein, Richard A. Palewicz* and *Walter R. Baron.*

For the respondent: *William G. Dillon, Simpson, Thacher & Bartlett,* New York, N.Y.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and of the Truth in Lending Act and the implementing regulation promulgated thereunder, and by virtue of the authority vested in it by said Acts, the Federal Trade Commission, having reason to believe that Insilco Corporation, a corporation, and Miles Homes, Inc., a corporation, hereinafter sometimes referred to as respondents, have violated the provisions of said Acts and the implementing regulation promulgated under the Truth in Lending Act, and it now appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint, stating its charges in that respect as follows:

PARAGRAPH 1. For purposes of this complaint, the following definitions shall apply:

a) The term "pre-cut housing" means homes sold to the general public by any of the Miles Homes Companies in the form of unassembled or partially assembled materials and components other than a package.

b) The term "package" means the materials and components for the plumbing, electrical or heating systems, kitchen cabinets not included with pre-cut housing, or tile or paint which any of the Miles Home Companies offer to purchasers of pre-cut housing.

PAR. 2. Respondent Insilco Corporation is a corporation organized, existing and doing business under and by virtue of the laws of the State of Connecticut, with its office and principal place of business located at 1000 Research Parkway, Meriden, Connecticut.

Respondent Insilco Corporation has numerous wholly-owned subsidiaries in various States of the United States which it collectively terms "Miles Homes Companies" and which includes, among others, Miles Homes, Inc.

Respondent Miles Homes, Inc. is a wholly-owned subsidiary of respondent Insilco Corporation, and is a corporation organized, existing and doing business under and by virtue of the laws of the State of Minnesota, with its office and principal place of business located at 4500 Lyndale Ave., North, Minneapolis, Minnesota.

Respondent Insilco Corporation by reason of its ownership of Miles Homes, Inc. has the power to and does control the acts and practices of Miles Homes, Inc.

PAR. 3. Respondents are now and for some time in the past have been engaged in the advertising, offering for sale and sale of pre-cut housing and packages for such housing to the general public.

PAR. 4. In the course and conduct of its business, as aforesaid, and by virtue of the control it exercises over respondent Miles Homes, Inc. by formulating, establishing and monitoring the financial and sales policies and operations of this subsidiary; through its wholly-owned corporate subsidiaries engaged in the sale of pre-cut housing in various States of the United States; and, through its other wholly-owned corporate subsidiaries which are distribution centers for pre-cut housing sold by respondents, respondent Insilco Corporation now causes, and for some time last past has caused, pre-cut housing to be transported from the states in which such distribution centers are located directly to purchasers located in various other States of the United States.

In the course and conduct of its business, as aforesaid, respondent Miles Homes, Inc. now causes, and for some time last past has caused, business papers and advertisements to be transmitted through the United States mail from respondent's place of business in Minnesota to members of the public located in various other States of the United States, and certain other advertisements to be inserted in newspapers of interstate circulation.

Therefore, each of the respondents now maintain, and at all times mentioned herein has maintained, a substantial course of trade in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act.

COUNT I

Alleging violations of Section 5 of the Federal Trade Commission Act, as amended, the allegations of Paragraphs One, Two, Three and Four hereof are incorporated by reference in Count I as if fully set forth verbatim.

PAR. 5. In the course and conduct of their housing business, as aforesaid, and for the purpose of inducing the public to purchase respondents' products, respondents have made, or are now making, certain statements and representations in advertising brochures and in advertising inserted in newspapers of interstate circulation.

Typical and illustrative of such statements and advertising representations, but not all inclusive thereof, are the following:

The only houses actually designed so they can be built by anyone who can drive a nail and follow simple instructions.

* * * * * * *

Build in spare hours without costly hired labor.

* * * * * * *

Your materials come pre-cut, ready to nail, with an excellent set of instructions designed for people with little or no previous building experience.

* * * * * * *

You can start the nailing and assembly within five minutes after you receive your home.

* * * * * * *

MILES PRECISION CUT HOMES

* * * * * * *

. . .a plan which combined financial assistance, all the materials, and easy to understand instructions. . .making it possible for any family to build their own home.

* * * * * * *

. . .We furnish precut building materials, step-by-step instructions, everything you need. . .inside and outside. Free delivery.

* * * * * * *

. . .You do not run out of material after you start building.

* * * * * * *

Our own fleet of trucks delivers your home in several loads, as you need it.

PAR. 6. By and through the use of the above-quoted statements and representations and others of similar import and meaning not expressly set cut herein, respondents have represented, or are now representing, directly or by implication that:

1. Pre-cut housing sold by respondents is easy to assemble and can be completely constructed by anyone.
2. Anyone can assemble respondents' pre-cut housing without utilizing the services of skilled building tradesmen during the course of construction.
3. Pre-cut housing sold by respondents is delivered to purchasers with all parts pre-cut to exact size with such accuracy that a purchaser need only to nail the parts in place.
4. Instructions furnished to purchasers by respondents for the assembly of pre-cut housing are designed for the specific style house ordered by each purchaser.
5. Instructions furnished to purchasers by respondents for the assembly of pre-cut housing are so simple that they can be easily followed by anyone.
6. Deliveries of materials and components of pre-cut housing sold by respondents are timed to meet the individual construction schedule needs of each purchaser.
7. Purchasers of respondents' pre-cut housing will be furnished adequate supplies of building materials to assure that the purchaser will not run short of materials or components during the course of construction.
8. Purchasers of respondents' pre-cut housing are not required to pay delivery charges for any of the materials or components for such housing purchased from respondents.

PAR. 7. In truth and in fact:

1. Pre-cut housing sold by respondents is not easy to assemble and cannot be completely constructed by any ordinary purchaser. In many instances purchasers, including those who have previous building construction experience, must hire skilled tradesmen to lay the foundation for the house.
2. Anyone cannot assemble respondents' pre-cut housing without using the services of skilled building tradesmen during the course of construction. In many instances, purchasers find it necessary to hire a carpenter, electrician or plumber for the construction of the house.
3. Pre-cut housing sold by respondents is not delivered to purchasers with all parts pre-cut to exact size with such accuracy that the parts need only to be nailed in place. Door and window openings, stairways, interior partition plates, interior wall studs, and hip, valley

and jack rafters are not pre-cut and must be measured and cut by purchasers during the construction of such housing.

4. Instructions furnished to purchasers by respondents for the assembly of pre-cut housing are not designed for the specific style house ordered by each purchaser. The instructions furnished are general in nature, and all purchasers receive an identical set of instructions regardless of the style house ordered.

5. Instructions furnished to purchasers by respondents for the assembly of pre-cut housing are not so simple that they can be easily followed by anyone. In many instances, purchasers are unable to interpret the instructions without the assistance of a carpenter, and instructions are not set out in the sequence of construction practice normally followed in the industry.

6. Deliveries of materials and components of pre-cut housing sold by respondents are not timed to meet the individual construction schedule needs of each purchaser. In many instances, deliveries are late, are made ahead of schedule, or are made at respondents' own convenience without regard to the schedule of delivery dates requested by purchasers.

7. Purchasers of respondents' pre-cut housing are not always furnished adequate supplies of building materials or components to assure that the purchaser will not run short of such materials or components during the course of construction. In some instances, an inadequate supply of nails, plywood or insulation is furnished. Respondents frequently delay, neglect, refuse or ignore making replacements of materials or components that are delivered to purchasers in damaged condition or where the delivery of the materials or components are not in accord with the purchaser's orders.

8. Purchasers of respondents' pre-cut housing are required to pay delivery charges for some of the materials or components for such housing. Delivery charges are added to purchasers' accounts when materials or components are shipped by carriers other than respondents' own trucks.

Therefore, the statements and representations as set forth in Paragraph Six above were and are false, misleading and deceptive.

PAR. 8. In the further course and conduct of their business, as aforesaid, and for the purpose of inducing the public to purchase respondents' pre-cut housing, respondents have made, or are now making, statements and representations in advertising brochures and in advertising inserted in newspapers of interstate circulation concerning the financial arrangements for the purchase of such housing.

Typical and illustrative of such statements and representations, but not all inclusive thereof, are the following:

You may build on your own lot. . .

* * * * * * *

Land need not be paid in full.

* * * * * * *

No Cash Needed. Monthly Payments: $84, including custom kitchen cabinets, plumbing, heating, electrical, tile and paint. . .

* * * * * * *

MILES PRECISION-CUT HOMES are recommended by banks, lending institutions and mortgage companies throughout the United States.

By and through the use of such statements and representations, respondents have failed to disclose the following material facts which, if known to consumers would be likely to affect their decision to respond to said advertising or to enter into negotiations with respondents which results, in many instances, in the purchase of pre-cut housing offered for sale by respondents:

1. That, in addition to the requirement that purchasers enter into a written agreement for the purchase of pre-cut housing, purchasers are also required to give respondents a mortgage note and first mortgage lien on the land used as the building site.
2. That the plumbing, heating or electrical systems, tile and paint, and kitchen cabinets are optional items for which respondents make substantial additional charges.
3. That respondents add delivery charges for materials and components shipped by carriers other than respondents' own trucks, and that such delivery charges always will be made for any "packages" ordered.
4. That respondents do not arrange long-term financing for individual purchasers from institutions that customarily furnish mortgage loans.
5. That the monthly payments are essentially in payment of the interest on the mortgage note purchasers are required to give respondents and reflect little or no reduction in the principal amount of the amount financed.

Therefore, respondents' failure to disclose such material facts were and are unfair, false, misleading and deceptive acts and practices.

PAR. 9. In the course and conduct of their aforesaid business and at all times mentioned herein, respondents have been and are now in substantial competition, in or affecting commerce, with corporations, firms and individuals in the sale of housing of the same general kind and nature as that sold by respondents.

PAR. 10. The use by respondents of the aforesaid unfair, misleading and deceptive statements, representations and practices has had and now has, the capacity and tendency to mislead members of the purchasing public into the purchase of substantial numbers of respondents' pre-cut housing.

PAR. 11. The aforesaid acts and practices of the respondents as herein alleged were and are all to the prejudice and injury of the public and respondents' competitors and constituted and now constitute unfair methods of competition, in or affecting commerce, in violation of Section 5 of the Federal Trade Commission Act.

COUNT II

Alleging violation of the Truth in Lending Act and the implementing regulation promulgated thereunder, and the Federal Trade Commission Act, the allegations of Paragraphs One, Two and Three hereof are incorporated by reference in Count II as if fully set forth verbatim.

PAR. 12. In the ordinary course and conduct of their business as aforesaid, respondents regularly extend and for some time in the past have regularly extended, consumer credit, as "consumer credit" is defined in Section 226.2(p) of Regulation Z, the implementing regulation of the Truth in Lending Act, duly promulgated by the Board of Governors of the Federal Reserve System.

PAR. 13. Subsequent to July 1, 1969, respondents, in the ordinary course and conduct of their business, and in connection with their credit sales, as "credit sale" is defined in Section 226.2(t) of Regulation Z, have caused, and are now causing, customers to execute a document entitled "Agreement," a retail installment contract, for the purchase of pre-cut housing. Concurrently with the agreement, respondents have furnished such customers with a "Separate Disclosure Statement of Credit Sale," a "notice to customers required by federal law" and an "Effect of Rescission."

PAR. 14. Subsequent to the Agreement referred to in Paragraph Thirteen, respondents made additional sales of materials, components or packages for the pre-cut housing (hereinafter sometimes referred to as "Additional Sales"). Such "Additional Sales" were a "credit sale" as defined in Section 226.2(t) of Regulation Z. Respondents provided no consumer credit cost disclosures required by Regulation Z.

PAR. 15. By and through the use of the "Agreement" referred to in Paragraph Thirteen, respondents, in some instances, have consummated a rescindable consumer transaction. Respondents, in some instances, have included the following language in the contract:

It is understood that this is not an order but a binding contract. After the Buyers' 3 day right of recission, provided by the Truth-in-Lending Law has expired, if the Buyers repudiate or countermand this contract prior to the delivery of any materials, Seller shall receive from Buyers reimbursement for all losses resulting from Buyers' breach, including the sum of $375.00 as and for Seller's loss of profit.

By and through the use of this quoted language, respondents have:

(1) Represented, directly or by implication, that customers will or may be liable for damages, penalties or any other charges if they exercise the right to rescind provided by Section 226.9 of Regulation Z on additional credit sales made pursuant to the "Agreement," contrary to the provisions of Section 226.9(d) of Regulation Z.

(2) Supplied additional information, not required by Regulation Z, which is stated so as to mislead or confuse the customers concerning his right to rescind the credit transaction, in violation of Section 226.6(c) of Regulation Z.

PAR. 16. By and through the use of the "Agreement" referred to in Paragraph` Thirteen a security interest, as "security interest" is defined in Section 226.2(gg) of Regulation Z, is or will be retained or acquired in real property which is or is expected to be used as the principal residence of the customer. Respondents have included the following language in the "Agreement":

SECTION D. It is agreed that the taking of a promissory note as evidence of Buyers' indebtedness to Seller shall not preclude Seller from filing a mechanic's lien in an amount specified herein for materials furnished and used in the improvement and alteration of Buyers' real estate and the Buyers consent and authorize the same.

However, in some cases, in the "Separate Disclosure Statement of Credit Sale" respondents have failed to properly identify the security interest as required by Section 226.8(b)(5) of Regulation Z.

PAR. 17. By and through the making of the "Additional Sale" referred to in Paragraph Fourteen respondents have made a "credit sale" as defined in Section 226.2(t) of Regulation Z. On these "Additional Sales," respondents have:

1. Failed in any consumer credit transaction to disclose the price at which respondent, in the regular course of business, offers to sell for cash the property or services which are the subject of the credit sale, and to describe that price as the "cash price," as required by Section 226.8(c)(1) of Regulation Z.
2. Failed to disclose the amount of any downpayment in money made in connection with any consumer credit transaction and to describe that amount as the "cash downpayment," as required by Section 226.8(c)(2) of Regulation Z.
3. Failed to disclose the "unpaid balance of cash price" to describe

the difference between the "cash price" and the "cash downpayment," as required by Section 226.8(c)(3) of Regulation Z.

4. Failed to disclose the "unpaid balance" to describe the sum of the "unpaid balance of cash price" and all other charges included in the amount financed but which are not part of the finance charge, as required by Section 226.8(c)(5) of Regulation Z.

5. Failed to disclose the amount of credit extended, and to describe that amount as the "amount financed," as required by Section 226.8(c)(7) of Regulation Z.

6. Failed to disclose the sum of all charges made to the customer which are required by Section 226.4 of Regulation Z to be included in the finance charge, and to describe that sum as the "finance charge," as required by Section 226.8(c)(8)(i) of Regulation Z.

7. Failed, in some instances, in consumer credit transactions to disclose accurately the sum of the cash price, all charges which are included in the amount financed but which are not part of the finance charge, and the finance charge, and to describe that sum as the "deferred payment price," as required by Section 226.8(c)(8)(ii) of Regulation Z.

8. Failed to disclose the "annual percentage rate" accurately to the nearest quarter of one percent, in accordance with Section 226.5(b) of Regulation Z, as required by Section 226.8(b)(2) of Regulation Z.

9. Failed to disclose the number, amount, and due dates or period of payments scheduled to repay the indebtedness, as required by Section 226.8(b)(3) of Regulation Z.

10. Failed to disclose the sum of the payments scheduled to repay the indebtedness, and to describe the sum as the "total of payments" as required by Section 226.8(b)(3) of Regulation Z.

11. Failed to make all disclosures required by Section 226.8(a) of Regulation Z.

Therefore, respondents have failed to make the consumer credit cost disclosures required by Section 226.8 of Regulation Z before the transaction is consummated, as required by Section 226.8(a) of the Regulation.

Par. 18. By and through the use of the "Additional Sales" referred to in Paragraph Fourteen, a security interest, as "security interest" is defined in Section 226.2(gg) of Regulation Z, other than a first lien or equivalent security interest, in some instances is or will be retained or acquired in real property which is used or expected to be used as the principal residence of the respondents' customers. Respondents' retention or acquisition of such security interest in said real property thereby entitles their credit customers to be given the right to rescind their transactions until midnight of the third business day following the consummation of the transaction or the date of delivery of all the disclosures in the manner and form required by Regulation Z, whichever is later, as required by Section 226.9(a) of Regulation Z.

Having consummated a rescindable consumer credit transaction, respondents or their representatives have, in many instances, made deliveries of materials, components or packages.

By and through their actions as alleged above, respondents have:

(1) Failed to give notice, in some instances, to each customer of the right to rescind the credit transaction by furnishing the customer with two copies of the "Notice to customers required by Federal law," set forth in Section 226.9(b) of Regulation Z, as required by Section 226.9(b) of Regulation Z.

(2) Failed to delay the making of deliveries, in some instances, to the residence of the customer until after the rescission period has expired, as required by Section 226.9(c)(4) of Regulation Z.

(3) Failed to provide customers, in some instances, with two copies of the "effect of rescission," set forth in Section 226.9(d) of Regulation Z, in the manner and form prescribed by Section 226.9(b) of Regulation Z.

PAR. 19. Respondents have, in some instances, furnished a notice of Right of Rescission in accordance with Section 226.9 of Regulation Z. Such notice was not printed in capital and lower case letters of not less than twelve (12) point bold-faced type as required by Section 226.9(b) of Regulation Z.

PAR. 20. Subsequent to July 1, 1969, respondents, in the ordinary course of their business as aforesaid and in connection with credit sales, have caused, and are causing, to be published, advertisements, as "credit sale" and "advertisement" are defined in Section 226.2 of Regulation Z, which advertisements aid, promote or assist, directly or indirectly, the extension of other than open end credit.

PAR. 21. Respondents, in certain of the above-mentioned advertisements, have stated and are stating the amount of downpayment, the amount of an installment payment or the period of repayment without also stating, as required by Section 226.10(d)(2) of Regulation Z, all the following terms:

(a) the cash price;

(b) the amount of the downpayment required or that no downpayment is required, as applicable;

(c) the number, amount and due dates or period of payments scheduled to repay the indebtedness if the credit is extended;

(d) the amount of the finance charge expressed as an annual percentage rate; and

(e) the deferred payment price (if applicable).

PAR. 22. Pursuant to Section 103(s) of the Truth in Lending Act, respondents' aforesaid failures to comply with the provisions of Regulation Z constitute violations of that Act, and, pursuant to Section 108 thereof, respondents have thereby violated the Federal Trade Commission Act.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondents named in the caption hereof, and the respondents having been furnished thereafter with a copy of a draft of complaint which the Chicago Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with violation of the Federal Trade Commission Act and the Truth in Lending Act and the implementing regulation promulgated thereunder; and

The respondents and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by the respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondents have violated said Acts, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent Insilco Corporation is a corporation organized, existing and doing business under and by virtue of the laws of the State of Connecticut, with its office and principal place of business located at 1000 Research Parkway, Meriden, Connecticut. It has numerous wholly-owned subsidiaries in various States of the United States which it collectively terms "Miles Homes Companies."

Respondent Miles Homes, Inc. is a wholly-owned subsidiary of respondent Insilco Corporation, and is a corporation organized, existing and doing business under and by virtue of the laws of the State of Minnesota, with its office and principal place of business located at 4500 Lyndale Ave., North, Minneapolis, Minnesota.

2. The Federal Trade Commission has jurisdiction of the subject

matter of this proceeding and of the respondents, and the proceeding is in the public interest.

ORDER

I

DEFINITIONS

For purposes of this order, the following definitions shall apply:

(a) The term "pre-cut housing" means homes sold to the general public by any of the Miles Homes Companies in the form of unassembled or partially assembled materials and components other than a package.

(b) The term "package" means the materials and components for the plumbing, electrical or heating systems, kitchen cabinets not included with pre-cut housing, or tile or paint which any of the Miles Homes companies offers to purchasers of pre-cut housing.

(c) The term "legal holiday" means any one of the following business holidays: New Year's Day, Washington's Birthday, Memorial Day, Independence Day, Labor Day, Veterans' Day, Thanksgiving Day, Christmas Day.

(d) The term "receipt" means three days following the date postmarked on written requests from purchasers provided that respondents are not precluded from establishing by other means the actual date of receipt of any written or oral request.

(e) The term "business days" means the days of the week that respondent Miles Homes, Inc. customarily conducts its business.

II

It is ordered, That respondents Insilco Corporation, a corporation, and Miles Homes, Inc., a corporation, and respondents' successors and assigns, and their officers, and respondents' representatives, agents and employees, directly or through any corporation, subsidiary, division or any other device, in connection with the advertising, offering for sale, sale or delivery of pre-cut housing, packages, homes or housing, in or affecting commerce as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

1. Representing, directly or by implication, by any means that:

(a) The only skill required for the assembly of respondents' pre-cut housing or packages is the ability to drive a nail or use a hammer, or that respondents' pre-cut housing or packages can be assembled by everyone without any construction skills or experience.

(b) Pre-cut housing or packages sold by respondents can in all cases be completely assembled without utilizing the services of a mason, carpenter, plumber, electrician or any other skilled building tradesman or other person experienced in building construction.

(c) Instructions furnished to purchasers for the assembly of respondents' pre-cut housing or packages are simple and are easily followed in all cases without any assistance from persons experienced in the building construction trades.

(d) No additional charge is made to purchasers for packages or other optional materials or components.

(e) All deliveries of materials and components for pre-cut housing or packages purchased from respondents are made without charge to purchasers.

2. Using the term "precision-cut" or any other words or terms of similar import or meaning which represents, directly or by implication, that materials or components for pre-cut housing or packages are delivered to purchasers accurately cut to size and fit when such materials or components require measuring and cutting after delivery to purchasers for assembly or installation in pre-cut housing purchased from respondents.

III

It is further ordered, That respondents, in connection with the advertising, offering for sale, sale or delivery of pre-cut housing, packages, homes or housing, shall include in all catalogues furnished to prospective purchasers, and shall furnish to each purchaser prior to the time such purchaser enters into any initial binding agreement for the purchase of respondents' pre-cut housing, a written statement that will set forth the following disclosures in a clear and conspicuous manner:

1. That purchasers who do not possess building construction skills or experience may find it necessary to hire or to otherwise secure the assistance of persons experienced in the building construction trades, such as a mason to lay the foundation, a carpenter to measure and cut materials and components to size for the house plan, a plumber to assemble and install plumbing and heating systems, and an electrician to install the electrical system, and that in some localities certain of such work is required by law to be performed by licensed tradesmen;

2. That purchasers who do not possess building construction skills or experience may find it necessary to hire or to otherwise secure the assistance of persons experienced in building construction to explain or interpret the instructions furnished by respondents;

3. That the land upon which respondents' pre-cut housing is to be built will be subject to a mortgage lien as security for a note in an amount that will cover all purchases made from respondents, and that

respondents may require that the purchaser furnish respondents with a copy of the deed showing ownership of such land;

4. That in those instances where the purchaser has not completed payment for the land upon which the pre-cut housing is to be built, respondents may require a copy of the contract evidencing sale of the land to the purchaser of such pre-cut housing and a permission-to-build agreement from the seller of the land;

5. That purchasers will be charged an additional amount for packages or other optional materials or components ordered when such are not included in the original purchase price;

6. That only specified deliveries will be made without charge to each purchaser and that other delivery charges which will vary depending on the number of orders a purchaser places, the quantity of materials purchased, the location of the shipper, and the method of shipment will be added to each purchaser's total indebtedness to respondents;

7. That respondents do not arrange long-term financing for individual purchasers from institutions that customarily furnish mortgage loans;

8. That the monthly payments made by purchasers to respondents will be, for the most part, in payment of the interest on the total amount financed with little, or no reduction in the total amount financed;

9. That materials or components delivered to purchasers should be inventoried and, in some cases must be sorted, after unloading;

10. That procedures, which respondents shall specifically identify and describe, have been established for the informal settlement of complaints and disputes concerning the shortage, omission or replacement of any material or component, and that purchasers will not be charged any fee by respondents for use of these procedures.

IV

It is further ordered, That respondents, in connection with the sale of pre-cut housing shall, at the time a purchaser enters into any initial contract or agreement for the purchase of such housing from respondents, inform each such purchaser orally of his right to cancel such contract or agreement and shall furnish to each such purchaser:

1. A fully completed copy of such purchase agreement or contract which is in the same language, *e.g.*, Spanish, as that principally used in the oral sales presentation and which shows the date of the transaction and contains the name and address of the seller, and in immediate proximity to the space reserved in the contract for the signature of the

purchaser and in boldface type of a minimum size of ten points, a statement in substantially the following form:

YOU, THE BUYER, MAY CANCEL THIS TRANSACTION AT ANY TIME PRIOR TO MIDNIGHT OF THE THIRD BUSINESS DAY, EXCLUDING SUNDAYS AND LEGAL HOLIDAYS, AFTER THE DATE OF THIS TRANSACTION. SEE THE ATTACHED NOTICE OF CANCELLATION FORM FOR AN EXPLANATION OF THIS RIGHT.

2. A completed form in duplicate, captioned "NOTICE OF CANCELLATION" attached to the purchase agreement or contract and easily detachable, and which shall contain in ten point boldface type the following information and statements in the same language, *e.g.*, Spanish, as that used in the contract:

NOTICE OF CANCELLATION

(enter date of transaction)
(Date)

YOU MAY CANCEL THIS TRANSACTION, WITHOUT ANY PENALTY OR OBLIGATION, WITHIN THREE BUSINESS DAYS FROM THE ABOVE DATE.

IF YOU CANCEL, ANY PROPERTY TRADED IN, ANY PAYMENTS MADE BY YOU UNDER THE CONTRACT OR SALE, AND ANY NEGOTIABLE INSTRUMENT EXECUTED BY YOU WILL BE RETURNED WITHIN 10 BUSINESS DAYS FOLLOWING RECEIPT BY THE SELLER OF YOUR CANCELLATION NOTICE, AND ANY SECURITY INTEREST ARISING OUT OF THE TRANSACTION WILL BE CANCELLED.

IF YOU CANCEL, YOU MUST MAKE AVAILABLE TO THE SELLER AT YOUR RESIDENCE, IN SUBSTANTIALLY AS GOOD CONDITION AS WHEN RECEIVED, ANY GOODS DELIVERED TO YOU UNDER THIS CONTRACT OR SALE; OR YOU MAY IF YOU WISH, COMPLY WITH THE INSTRUCTIONS OF THE SELLER REGARDING THE RETURN SHIPMENT OF THE GOODS AT THE SELLER'S EXPENSE AND RISK.

IF YOU DO MAKE THE GOODS AVAILABLE TO THE SELLER AND THE SELLER DOES NOT PICK THEM UP WITHIN 20 DAYS OF THE DATE OF YOUR NOTICE OF CANCELLATION, YOU MAY RETAIN OR DISPOSE OF THE GOODS WITHOUT ANY FURTHER OBLIGATION. IF YOU FAIL TO MAKE THE GOODS AVAILABLE TO THE SELLER, OR IF YOU AGREE TO RETURN THE GOODS TO THE SELLER AND FAIL TO DO SO, THEN YOU REMAIN LIABLE FOR PERFORMANCE OF ALL OBLIGATIONS UNDER THE CONTRACT.

TO CANCEL THIS TRANSACTION, MAIL OR DELIVER A SIGNED AND DATED COPY OF THIS CANCELLATION NOTICE OR ANY OTHER WRITTEN NOTICE, OR SEND A TELEGRAM TO *(Name of Seller)*, AT *(Address of seller's place of business)* NOT LATER THAN MIDNIGHT OF *(Date)*.

I HEREBY CANCEL THIS TRANSACTION.

(Date)

(Buyer's Signature)

3. The requirements set out in subparagraphs 1 and 2 above, do not apply in any case in which the purchaser is accorded the right of rescission by the provisions of the Consumer Credit Protection Act (15 U.S.C. 1635) or regulations issued pursuant thereto.

V

It is further ordered, That respondents, in connection with the sale or delivery of pre-cut housing, packages, homes or housing shall:

1. Upon the receipt of a purchaser's written request for delivery of materials or components, acknowledge each such request within ten (10) business days and notify the purchaser in writing within thirty (30) days of the receipt of such request of the date on which such delivery will be scheduled; *provided,* that if a purchaser has not furnished respondents with satisfactory documentary evidence that all conditions precedent to such purchaser's contractual right to the requested delivery have been fulfilled and that the construction of such purchaser's house has progressed to the point where delivery of the requested materials or components is appropriate, then respondents need not arrange for the requested delivery but must advise such purchasers, within thirty (30) days of the receipt of the request, of the reason or reasons why the request for delivery will not be honored;

2. Schedule the delivery date referred to in subparagraph 1 above for a date within ten (10) business days of the date requested by the purchaser; *provided,* that if the requested delivery date is less than thirty (30) days from the date of receipt by respondents of the request for delivery, then respondents shall schedule delivery for a reasonable time thereafter;

3. Notify each purchaser at the time the initial purchase contract is made where purchasers are directed to address inquiries or complaints concerning:

(a) the purchaser's contractual agreement with respondents,

(b) the delivery of materials or components,

(c) shortages, omissions or replacement of materials or components, and

(d) the construction, assembly and installation of pre-cut housing or packages.

4. Furnish to each purchaser a reasonable number of pre-addressed post cards for the purpose of submitting the inquiries or complaints referred to in subparagraph 3 above;

5. Acknowledge receipt of each written inquiry or complaint received from purchasers within ten (10) business days, and notify each

such purchaser in such acknowledgment of the approximate date on which response to the inquiry or complaint will be furnished; such response shall be in writing and no later than thirty (30) days from the date of the receipt of the inquiry or complaint;

6. Make a disposition relating to the purchaser's inquiry or complaint on or before the expiration of the thirty (30) day period referred to in subparagraph 5 above. Respondents' response to an inquiry or complaint relating to the shortage, omission or replacement of any material of component shall state:

(a) whether or not respondents will furnish such material or component,

(b) the date on which delivery of the requested material or component will be scheduled, which date shall not be unreasonably distant in the future, and

(c) the reason or reasons why respondents will not furnish the requested material or component, if such be the case.

Provided, that this subparagraph 6 shall not be construed to preclude respondents from furnishing any purchaser with a credit for the purchase price and delivery charges of any material or component or from taking other remedial action with respect to any material or component.

7. Designate a single focal point within the operations of Miles Homes Companies for the receipt of complaints which have not been resolved to the satisfaction of any purchaser under the procedures set out in subparagraphs 3, 4, 5 and 6 above, and notify each such purchaser at the time the response is made under subparagraph 6 above of the focal point and individual to whom such disputed complaints are to be directed;

8. Acknowledge, in writing, each complaint received pursuant to subparagraph 7 above within ten (10) business days of the date such complaint was received and within thirty (30) days of receipt of such complaint notify the purchaser in writing of the disposition made with respect to such dispute;

9. Establish a procedure whereby disputes with purchasers concerning the shortage, omission or replacement of any material or component which cannot be resolved on a mutually agreeable basis within forty (40) business days after the receipt of a complaint from a purchaser under the procedures described in subparagraphs 7 and 8 above, are promptly referred to and reviewed by an officer of Insilco Corporation. Such officer shall: be an officer who is not responsible for the day-to-day operation of Miles Homes, Inc. or for the day-to-day operation of any of the Miles Homes Companies; fairly and expedi-

tiously settle each dispute no later than thirty (30) business days from the date the dispute is received by the officer; and, notify the purchaser promptly, and in writing, of the disposition of the dispute;

10. Specifically perform without unreasonable delay and in good faith in each instance where a complaint or dispute is resolved in favor of a purchaser through the procedures in Part V of the order;

11. Use good faith efforts to meet each and every delivery date scheduled under Part V of the order, provided that in the event respondents are unable to make such deliveries as required due to intervening circumstances beyond their control such as labor strike, supplier failure to deliver, or unsuitable weather conditions, then respondents' obligation to deliver shall be suspended for the duration of such intervening circumstance and purchasers shall be notified in writing of the reason or reasons why delivery will be delayed.

Provided, however, in the event respondents adopt open-end credit plans under Section 226.7 of Regulation Z, respondents may petition the Commission to modify Part V of this order to make the time periods consistent with the time periods required under Sections 226.7 and 226.14 of Regulation Z (12 CFR 226).

VI

It is ordered, That respondents Insilco Corporation, a corporation, and Miles Homes, Inc., a corporation, and respondents' successors, assigns, officers, representatives, agents and employees, directly or through any corporation, subsidiary, division or any other device, in connection with any extension of or arrangement for consumer credit, or any advertisement to aid, promote or assist, directly or indirectly any extension of or arrangement for consumer credit, as "consumer credit" and "advertisement" are defined in Regulation Z (12 CFR 226) of the Truth in Lending Act 15 U.S.C. 1601-65 (1970), *as amended,* 15 U.S.C. 1601-65(a) (Supp. IV) 1974, do forthwith cease and desist from:

1. Failing in any consumer credit transaction to disclose the price at which respondents, in the regular course of business, offer to sell for cash the property or services which are the subject of the credit sale, and to describe that price as the "cash price," as required by Section 226.8(c)(1) of Regulation Z.

2. Failing to disclose the amount of any downpayment in money made in connection with any consumer credit transaction and to describe that amount as the "cash downpayment," as required by Section 226.8(c)(2) of Regulation Z.

3. Failing to disclose the "unpaid balance of cash price" to describe

the difference between the "cash price" and the "cash downpayment," as required by Section 226.8(c)(3) of Regulation Z.

4. Failing to disclose the "unpaid balance" to describe the sum of the "unpaid balance of cash price" and all other charges included in the amount financed but which are not part of the finance charge, as required by Section 226.8(c)(5) of Regulation Z.

5. Failing to disclose the amount of credit extended, and to describe that amount as the "amount financed," as required by Section 226.8(c)(7) of Regulation Z.

6. Failing to disclose the sum of all charges made to the customer which are required by Section 226.4 of Regulation Z to be included in the finance charge, and to describe that sum as the "finance charge," as required by Section 226.8(c)(8)(i) of Regulation Z.

7. Failing to disclose accurately the sum of the cash price, all charges which are included in the amount financed but which are not part of the finance charge, and the finance charge, and to describe that sum as the "deferred payment price," as required by Section 226.8(c)(ii) of Regulation Z.

8. Failing to disclose the "annual percentage rate" accurately to the nearest quarter of one percent, in accordance with Section 226.5 of Regulation Z, as required by Section 226.8(b)(2) of Regulation Z.

9. Failing to disclose the number, amount, and due dates or period of payments scheduled to repay the indebtedness, as required by Section 226.8(b)(3) of Regulation Z.

10. Failing to disclose the sum of the payments scheduled to repay the indebtedness, and to describe the sum as the "total payments" as required by Section 226.8(b)(3) of Regulation Z.

11. Stating, utilizing, or placing any information or explanation not required or authorized by Regulation Z in a manner which might tend to mislead or confuse the customer or contradict, obscure, or detract attention from the information required by Regulation Z to be disclosed, as required by Section 226.6(c) of Regulation Z.

12. Failing to give notice to each customer of the right to rescind the credit transaction by furnishing the customer with two copies of the "Notice to customers required by Federal law," set forth in Section 226.9(b) of Regulation Z, as required by Section 226.9(b) of Regulation Z, and in the required type size set out in Section 226.9(b) of Regulation Z.

13. Failing to delay the making of deliveries to the residence of the customer until after the rescission period has expired, as required by Section 226.9(c)(4) of Regulation Z.

14. Failing to provide customers with two copies of the "effect of

rescission," set forth in Section 226.9(d) of Regulation Z, in the manner and form prescribed by Section 226.9(b) of Regulation Z.

15. Failing to furnish customers with disclosures prescribed by Section 226.8 of Regulation Z at the time and in the manner and form required by that section.

16. Failing to furnish customers with a duplicate of the instrument or a statement by which the disclosures prescribed by Section 226.8 of Regulation Z are made, and on which the creditor is identified, as required by Section 226.8(a) of Regulation Z.

17. Failing to disclose a description or identification of the type of security interest held or to be retained or acquired by the creditor in connection with the extension of credit, as required by Section 226.8(b)(5) of Regulation Z.

18. Representing in any advertisement, directly or by implication, that no downpayment is required, the amount of the downpayment or the amount of any instalment payment, either in dollars or as a percentage, the dollar amount of any finance charge, the number of instalments or the period of repayment, or that there is no charge for credit, unless all of the following items are clearly and conspicuously stated, in terminology prescribed under Section 226.8 of Regulation Z, as required by Section 226.10(d)(2) of Regulation Z:

(a) the cash price;

(b) the amount of the downpayment required or that no downpayment is required, as applicable;

(c) the number, amount and due dates or period of payments scheduled to repay the indebtedness if the credit is extended;

(d) the amount of the finance charge expressed as an equal percentage rate; and

(e) the deferred payment price if applicable.

Provided, that respondents may make disclosures for open-end credit under Section 226.7 of Regulation Z without regard to any provisions required under Section 226.8 above of Regulation Z.

19. Failing, in any consumer credit transaction or advertisement, to make all disclosures determined in accordance with Section 226.4 and Section 226.5 of Regulation Z at the time and in the manner, form, and amount required by Sections 226.6, 226.7, 226.8, 226.9 and 226.10 of Regulation Z.

VII

It is further ordered, That respondents in connection with the sale or delivery of pre-cut housing, packages, homes or housing shall:

1. Furnish each purchaser of respondents' pre-cut housing or

packages with an itemized statement of account at least once every six months which sets forth to such date all purchases, credits, payments credited to interest, payments credited to principal, and current balance owed to respondents.

2. Secure from each purchaser of respondents' pre-cut housing a written acknowledgment which shall state the following information:

(a) That the disclosures referred to in Part III of this order were received.

(b) The date on which the disclosures referred to in Part III of this order were received.

3. Notify each existing and future purchaser of respondents' obligations under Part V of this order.

VIII

It is further ordered, That respondents shall maintain and, upon reasonable notice, provide access to the Commission or its representatives for the purpose of inspection and copying, for a period of three years from the date each complaint is received:

1. All complaints made to respondents by purchasers concerning the shortage, omission, replacement or delivery of materials, components and packages.

2. All correspondence and documents regarding complaints, and disputes made by purchasers concerning the shortage, omission, replacement or delivery of materials, components and packages, including all records concerning the disposition of such complaints and disputes.

IX

It is further ordered, That no provision of this order shall be construed in any way to annul, invalidate, repeal, terminate, modify or exempt respondents from complying with agreements, orders, regulations, or building codes or directives of any kind issued or required by any governmental agency, or any other state or local laws, or act as a defense to actions instituted by municipal or state regulatory agencies, or be construed as a waiver of legal rights either party may have which vary from state to state.

X

It is further ordered, That respondents shall within thirty (30) days of the effective date of this order distribute a copy of the order to:

1. Each of respondents' operating divisions and subsidiaries

engaged in the advertising, offering for sale, sale or delivery of pre-cut housing, packages, homes or housing.

2. All personnel of the respondent corporations and of the operating divisions and subsidiaries of all of respondents' corporations who are engaged or who may hereafter become engaged in the consummation of any extension of consumer credit, and in the advertising, offering for sale, sale or delivery of respondents' pre-cut housing, packages, homes, or housing and that in connection with such distribution, respondents shall secure a signed statement from each person acknowledging receipt of a copy of this order.

It is further ordered, That respondents notify the Commission at least 30 days prior to any proposed change in the corporate respondents such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporations which may affect compliance obligations arising out of the order.

It is further ordered, That the respondents herein shall within sixty (60) days after service upon them of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied with this order.

IN THE MATTER OF

XEROX CORPORATION

MODIFYING ORDER IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket 8909. Final Order, July 29, 1975 — Modifying Order, April 20, 1978

This order modifies an order to cease and desist issued July 29, 1975, 40 FR 42203, 86 F.T.C. 364, by deleting the words *"in camera"* from Paragraph IV C.(9) thereof.

ORDER MODIFYING ORDER TO CEASE AND DESIST

On July 29, 1975, the Federal Trade Commission issued a consent order in the above-referenced matter. 86 F.T.C. 364 (1975).

Section 5(b) of the Federal Trade Commission Act provides that the Commission may at any time, after notice and opportunity for hearing, reopen and alter, modify or set aside, in whole or in part, any order issued by it, whenever in the opinion of the Commission conditions of fact or law have so changed as to require such action or if the public interest shall so require.

On January 19, 1978, the Commission issued its order to respondent to show cause why the Commission should not alter or modify the July 29, 1975 order so as to delete the words *"in camera"* from Paragraph IV C.(9) thereof.

On March 6, 1978, respondent filed an answer that did not oppose the proposed modification. Section 3.72(b)(3) of the Commission's Rules provides that if an order to show cause is not opposed the Commission may, in its discretion, decide the matter on the basis of that order and the answer thereto.

Accordingly, *it is ordered,* That the matter be reopened, and that Paragraph IV C.(9) of the order of July 29, 1975, be modified to read as follows:

> If *Xerox* grants a license under *order patents* either pursuant to the terms of Paragraph II of this order or otherwise, the license agreement shall contain the irrevocable covenant of the licensee to license such of its *patents* as are licensed to *Xerox* on reasonable terms and conditions (including the license to itself of its licensees' *patents* or *improvement patents*) to any other person who is entitled to a license from *Xerox* pursuant to Paragraph II of this order, Provided That such license need not be effective prior to the effective date of the licensee's license to *Xerox.* Within 60 days following execution of a license agreement subject to this Paragraph IV C(9), *Xerox* shall submit to the Commission a copy thereof.

IN THE MATTER OF

FIRESTONE PHOTOGRAPHS, INC., ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2921. Complaint, April 20, 1978 — Decision, April 20, 1978

Consent order requiring a Columbus, Ohio, promoter and seller of photographic equipment and supply franchises, among other things, to cease misrepresenting its repurchase plan, potential profits, connection or affiliation with others, and the training and business assistance provided franchisees. The order further requires the firm to make full and timely disclosures and provide prescribed data regarding any cooling-off periods, cancellation and refund rights, and the financial history of both the corporation and previous franchisees. The firm is additionally required to maintain specific records and to institute a surveillance program designed to ensure compliance with the terms of the order.

Appearances

For the Commission: *Melvin H. Wolovits* and *Noble F. Jones.*

For the respondents: *Harris, Strip, Fargo, Schulman & Hoppers,* Columbus, Ohio.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Firestone Photographs, Inc., a corporation, Firestone Photo Co., a corporation, and Daniel Firestone, individually and as an officer of said corporations, hereinafter sometimes referred to as respondents, have violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. For the purpose of this complaint and the Agreement Containing a Consent Order to Cease and Desist entered into by the Federal Trade Commission and respondents, the following definitions shall apply:

(1) The term "franchise" shall mean any continuing commercial relationship created by written agreement or understanding where:

(a) A person offers, sells or distributes goods or commodities manufactured, processed or distributed by respondent; and

(b) Respondent directly or impliedly represents, either orally or in writing, that it will assist such person in such person's organization, promotional activities, management, marketing plan, method of operation or other business activities.

(2) The term "franchisee" shall mean any person to whom a franchise is granted.

(3) The term "business day" means any day other than Saturday, Sunday, or the following national holidays: New Year's Day, Washington's Birthday, Memorial Day, Independence Day, Labor Day, Columbus Day, Veterans' Day, Thanksgiving, and Christmas.

(4) The terms "material," "material fact," and "material change" shall include any fact, circumstance, or set of conditions which would have a substantial likelihood of influencing a reasonable franchisee or a reasonable prospective franchisee in the making of a decision relating to respondents' franchise business or which would have any significant financial impact on a franchisee or a prospective franchisee.

(5) The term "bona fide wholesale price" refers to a price which constitutes a fair payment for goods purchased at the same level of distribution and no part of which constitutes payment for the right to enter into or continue in respondents' franchise business.

PAR. 2. Respondent, Firestone Photographs, Inc., is a corporation organized, existing and doing business under and by virtue of the laws of the State of Ohio, with its principle office and place of business located at 168 North Third St., Columbus, Ohio.

Respondent, Firestone Photo Co., is a corporation organized, existing and doing business under and by virtue of the laws of the State of Ohio, with its principle office and place of business located at 168 North Third St., Columbus, Ohio.

Respondent, Daniel Firestone, is an individual and officer of respondent corporation. He formulates, directs and controls the acts and practices of said business entity, including the acts and practices hereinafter set forth. His address is 168 North Third St., Columbus, Ohio.

PAR. 3. Respondents are now, and for some time in the past have been engaged in the advertising, offering for sale, and sale of franchises which authorize franchisees to sell to members of the public items of merchandise, including but not limited to Kodak film and Firestone Photographs, Inc. prepaid film processing envelopes.

PAR. 4. In the course and conduct of their business, respondents for some time last past have caused, said products, when sold, to be shipped from their place of business in the State of Ohio to purchasers thereof located in various other states of the United States. In addition, in the course and conduct of their business, respondents have disseminated and caused to be disseminated in newspapers of interstate circulation, advertisements designed to be read by persons residing outside the State of Ohio and intended to induce such persons to enter into contractual agreements with respondents to purchase franchises and products from respondents. Respondents also introduced into interstate circulation, through the instrumentality of the United States mails, promotional materials, circulars, business papers and other written instruments and communications with the result and effect that members of the public residing outside the State of Ohio, in various other States of the United States did, in fact, purchase respondents' franchises and products, thereby placing respondents' business in commerce within the intent and meaning of Section 5 of the Federal Trade Commission Act, as amended.

Respondents have maintained, and at all times mentioned herein maintained, a substantial course of trade in distributorships and products, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act.

PAR. 5. In the course and conduct of their business as above mentioned and for the purpose of inducing the purchase of their franchises and products, respondents Firestone Photographs, Inc., a corporation, Firestone Photo Co., a corporation, and Daniel Firestone, individually and as an officer of said corporations, engaged in a program of recruitment of franchisees for their franchise program. As part of this program respondents have made numerous statements and representations in promotional materials and in newspaper advertisements.

Typical and illustrative of such statements, but not all inclusive thereof, are the following:

No selling or soliciting required

* * * * * * *

A 100% GUARANTEE FOR 12 MONTHS

* * * * * * *

QUALIFIED INDIVIDUAL MALE OR FEMALE

* * * * * * *

Very Conservative Profit Projections. . .
10 Locations . . . $ 5,148 per year
50 Locations . . . $25,740 per year

PAR. 6. By and through the use of the aforesaid statements and others of similar import not specifically set forth herein, respondents represent directly or by implication that:

(1) A person can expect to earn between $5,148 and $25,740 or more per year by devoting part time to his franchise.

(2) There is no selling or soliciting required of a franchisee.

(3) Respondents will repurchase and refund a franchisee's entire investment for any reason within a twelve (12) month period.

(4) Respondents are selective with regard to persons qualified to become franchisees.

PAR. 7. In truth and in fact:

(1) A person cannot expect to earn between $5,148 and $25,740 per year by devoting part time to his franchise. Such earnings claims are greatly in excess of the profit that will accrue in a great majority of cases, no matter how much time is devoted to the distributorship.

(2) Selling or soliciting is required of a franchisee if profitable locations are to be obtained.

(3) Respondents have in few cases, if ever, repurchased and refunded a franchisee's entire investment within a twelve (12) month period.

(4) In order to purchase a franchise from respondents, the only qualification existing is that the purchaser have sufficient funds for the franchise investment.

Therefore, the statements and representations as set forth in Paragraphs Five, Six and Seven were and are false, misleading and deceptive.

PAR. 8. In the further course and conduct of their business aforesaid and in furtherance of their purpose of inducing the purchase of their franchises, respondents direct various newspapers to print advertisements containing the corporate logo of Kodak Corporation. The use of this logo in newspaper advertising and on other printed matter disseminated by respondents represents, directly or by implication, that respondents are closely affiliated with the said corporation.

In fact, respondents are not closely affiliated, nor are they affiliated in any way with the said corporation. Rather, the relationship between respondents and the said corporation is basically that of supplier-purchaser.

Therefore, the acts and practices set forth above were and are, false, misleading and deceptive.

PAR. 9. In the further course and conduct of their business as aforesaid and for the purpose of inducing the purchase of their franchise and products, respondents, their agents, representatives or employees, or any of them, have made representations, either orally or in writing, that:

(1) A franchisee will earn between $5,200 and $52,000 or more per year.

(2) A distributor can recover his entire initial investment within a one year period.

(3) Respondents will obtain and set up profitable sales producing locations in high traffic business establishments and retail store outlets, such as supermarkets and drug stores.

(4) Respondents will obtain and set up permanent locations in business establishments and retail store outlets for franchisees.

(5) Business establishments and retail store outlets will be obtained and set up shortly after franchisees sign a contract or purchase agreement.

(6) Respondents will train and assist franchisees in obtaining and setting up new permanent business establishments and retail store outlets.

PAR. 10. In truth and in fact:

(1) Few, if any, of respondents' franchisees have earned $5,200 per year or more.

(2) Few, if any, of respondents' franchisees have recovered, from the operation of the franchise, their entire initial investment within one year.

(3) The type of business locations and retail store outlets obtained and set up by respondents are not located in high traffic sales producing locations such as supermarkets and drug stores.

(4) Respondents do not obtain and set up permanent business locations and retail store outlets for franchisees. In fact, in a substantial number of instances, business locations and retail store outlets obtained and set up by respondents, terminate their relationship with the franchisee in sixty (60) days or less from the day they commence operating and through no fault of the franchisee.

(5) Business locations and retail store outlets are not obtained and set up shortly after franchisees sign their contracts. Often there are protracted delays caused by respondents.

(6) Respondents in few instances, if any, assist franchisees in obtaining and setting up additional permanent business locations.

Therefore, the statements and representations as set forth in Paragraphs Nine and Ten were, and are, false, misleading and deceptive.

PAR. 11. In the further course and conduct of its business, respondents and prospective franchisees enter into franchise contracts and purchase agreements. In a substantial number of these instances, the prospective franchisee is unemployed and without the assistance of counsel and enters said contracts in a state other than Ohio.

PAR. 12. Respondents, as a part of said franchise contract or purchase agreement, include the following "venue waiver" provision:

> The parties further agree that this Agreement shall be deemed to have been executed in the State of Ohio and to submit any dispute or cause of action which may arise, solely to the Courts of the State of Ohio.

PAR. 13. The venue waiver provision is not a bargained-for part of the franchise contract or purchase agreement and is not generally understandable to persons without legal background or experience. By requiring franchisees to waive statutory venue provisions, respondents have deprived and is depriving them of rights otherwise available to them, under the laws of the state where in fact the franchise contract or purchase agreement was executed. Therefore, such use of the "venue waiver" provision is unfair.

PAR. 14. The use by respondents of the aforesaid false, misleading and deceptive statements, representations, acts and practices has been, and now has the tendency and capacity to mislead and deceive members of the public into the erroneous and mistaken belief that said statements and representations were and are true and complete, and induce the purchase of respondents' franchises and products by reason of said erroneous and mistaken beliefs, and into the assumption of obligations and the payment of monies, as a result thereof, which they might otherwise not have incurred.

PAR. 15. In the course and conduct of their aforesaid business, and at all times mentioned herein, respondents have been, and now are, in substantial competition in or affecting commerce, with corporations, firms and individuals engaged in the sale of franchises and products of the same general kind and nature as those sold by respondents.

PAR. 16. The aforesaid acts and practices of respondents, as herein alleged, were and are all to the prejudice and injury of the public and of respondents' competitors and constituted, and now constitute, unfair and deceptive acts or practices in commerce in violation of Section 5 of the Federal Trade Commission Act, as amended.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondents named in the caption hereof, and the respondents having been furnished thereafter with a copy of a draft of complaint which the Cleveland Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with violation of the Federal Trade Commission Act; and

The respondents and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondents have violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter pursuant to Section 2.34(b) of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent Firestone Photographs, Inc. is a corporation organized, existing, and doing business under and by virtue of the laws of the State of Ohio, with its office and principal place of business located at 168 North Third St., Columbus, Ohio.

Respondent Firestone Photo Co. is a corporation organized, existing, and doing business under and by virtue of the laws of the State of Ohio, with its office and principal place of business located at 168 North Third St., Columbus, Ohio.

Respondent Daniel Firestone is an officer of said corporations. He formulates, directs, and controls the policies, acts, and practices of said corporations, and his address is the same as that of said corporations.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

ORDER

I

It is ordered, That respondent Firestone Photographs, Inc., a corporation, its successors and assigns, and its officers, agents. representatives, and employees, Firestone Photo Co., a corporation, and its successors and assigns, and its officers, agents, representatives, and employees, and Daniel Firestone, individually and as an officer of said corporations, directly or through any other corporation, subsidiary, division, or other device, in connection with the advertising, offering for sale, sale, contracting, or other promotion of any franchise, distributorship, dealership, license, goods, services, or commodities manufactured, processed or distributed in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, do forthwith cease and desist from:

A. Representing directly or by implication through the use of any means that:

(1) Selling or soliciting is not required to operate a franchise;

(2) Respondents have a connection or affiliation with any manufacturer of products or services available to franchisees, other than that of supplier-purchaser; or misrepresenting, in any manner, respondents' business connection, affiliation or association with other firms, organizations, groups, or individuals;

(3) Prospective franchisees will receive advice, assistance or training for organizing, maintaining or operating their franchise, or misrepresenting in any manner the quality, amount and nature of assistance to be provided by respondents, except as provided for in Paragraph II (9) of this order;

(4) Prospective franchisees will be provided, as a part of its franchise, specific types of business locations or retail store outlets, such as supermarkets or drug stores; or misrepresenting, in any manner, the desirability of any specific business location or retail store outlet to be provided, as stated hereinabove;

(5) Prospective franchisees must be qualified, possess certain skills or experiences in order to be selected or accepted as a franchisee.

B. Using in an advertisement any logo, trademark or seller's emblem of the Eastman Kodak Company or any other company or organization other than respondents; *provided*, that, if respondents use in an advertisement the trade name of any company other than its own, that trade name shall not appear in boldface type and in no greater than two (2) type point sizes smaller than respondents' name.

C. Providing respondents' franchisees with point of sale display racks which fail to disclose clearly and conspicuously respondents' name and its product or service being offered for sale.

D. From making, directly or by implication, orally or in writing, any representation with respect to a prospective franchisee's potential sales, income, gross or net profit, or with respect to a prospective franchisee's potential return of their purchase price within a stated period of time, except as provided for in Paragraph II (7) of this order.

E. Representing, directly or by implication, orally or in writing, any limitation with respect to the county or court in which a franchisee may institute a lawsuit against respondents. This provision shall not preempt any rule of law which limits choice of county or court.

F. Representing, directly or by implication, orally or in writing, that respondents will repurchase, guarantee or otherwise refund (hereinafter referred to as repurchase plan), for any reason, any amount of money paid to respondents in connection with the purchase of respondents' franchises, unless in immediate conjunction with the representation, and in each franchise contract or purchase agreement in no less than eight (8) point type size, all conditions and terms of the repurchase plan are clearly and conspicuously disclosed in simple and readily understood language. Such disclosure shall include the following information:

(1) Those products, services or franchise fees included in the repurchase plan, and all exceptions and exclusions of the repurchase plan;

(2) The step by step procedure which the franchisee must take in order to obtain performance under the repurchase plan, including the expenses he must incur; and

(3) The time or period of time in which respondents will perform any obligation under the repurchase plan.

G. Making any claim or representation, either orally or in writing, for which the respondents do not have in their possession valid substantiating data, which data shall be made available to prospective franchisees, and to the Commission or its staff upon five (5) days written notice.

II

It is further ordered, That each prospective purchaser of respondents' franchises receive, at least fifteen (15) business days prior to: (1) the execution of any contract, purchase agreement or other binding obligation in connection with the sale of respondents' franchise; or (2) the payment by or on behalf of the prospective purchaser of any consideration in connection with the sale or proposed sale of respondents' franchise, which ever occurs first:

A. The completed contract, purchase agreement, or other obligation proposed to be used;

B. A copy of the Federal Trade Commission's News Release issued by the Commission in conjunction with its provisional acceptance of this order; and

C. A single disclosure statement, which shall not contain any promotional claims or other information not required by this order. Provided this does not preclude respondents from giving explanatory information in separate literature so long as such explanatory information is not inconsistent with the disclosure statement required by this part.

The statement shall carry a distinctive and conspicuous cover sheet with the following notice (and no other) imprinted thereon in boldface type of not less than 10 point size:

INFORMATION FOR PROSPECTIVE DISTRIBUTORS REQUIRED BY FEDERAL TRADE COMMISSION

This package of information is provided for your own protection. It is in your best interest to study it carefully before making any commitment.

If you do sign a contract, you may cancel it, and obtain a full refund of any money paid, for any reason within ten (10) business days after signing. Details appear on the contract itself.

The information contained herein has not been reviewed or approved by the Federal Trade Commission. A false, inaccurate or incomplete statement may constitute a violation of Federal law and should be reported to the Federal Trade Commission in Washington, or the Federal Trade Commission's Regional Office nearest you. In addition, there may be laws concerning franchising within your state. It is recommended that you contact your state government for its requirements or regulations.

Such disclosure statement shall contain the following information as of the close of the respondents' last fiscal year. After the close of each fiscal year, respondents shall have a period not exceeding ninety (90) days to prepare a revised disclosure statement, and following such ninety (90) days may distribute only the revised prospectus and no other. Irrespective of the above, a revised prospectus must be prepared and distributed upon the occurrence of any material change in respondents or relating to the franchise business of respondents. As used in this order, the term "fiscal year" shall mean respondents' fiscal year:

(1) The official name(s) and address(es) of respondents and the name under which respondents are doing business.

(2) The business experience of respondents, including the length of time respondents have conducted a business of the type to be operated by the franchisee, or have granted franchises for such business, or have granted franchises, in other lines of business.

(3) Where such is the case, a statement that the respondents or any of its directors, stockholders owning more than ten percent of the stock, or chief executive officers:

(a) Has been held liable in a civil action, convicted of a felony, or pleaded nolo contendere to a felony charge in any case involving fraud, embezzlement, fraudulent conversion, or misappropriation of property during the previous seven (7) fiscal years; or

(b) Is subject to any currently effective court injunctive or restrictive order or ruling relating or affecting franchise activities of respondents as a result of action by any public agency or department; or

(c) Has filed bankruptcy or been associated with management or any company that has been involved in bankruptcy or reorganization proceedings; or

(d) Is, or has been, a party to any cause of action brought by a franchisee against respondents.

Such statement shall set forth the identity and location of the court, date of conviction or judgment, any penalty imposed or damages assessed, and the date, nature and issuer of each such order or ruling.

(4) The financial history of the corporate respondents, including balance sheets and profit and loss statements for the most recent five-year period; and a statement of any material changes in the financial condition of the corporate respondent since the date of such financial statement.

(5) A statement of the total funds which must be paid to respondents in order to obtain or commence the franchise operation, and the total amount of said funds which is represented by, based upon a bona fide wholesale price, the following:

(a) Film;

(b) Prepaid film processing mailing envelopes;

(c) Other products individually identified.

(6) A statement disclosing with respect to respondents:

(a) The total number of franchises operating at the end of the preceding fiscal year;

(b) The names, addresses, and telephone numbers of the ten franchisees nearest the prospective franchisee's intended location;

(c) The number of franchises voluntarily terminated by franchisees during the preceding fiscal year; and

(d) The number of franchises repurchased or cancelled by respondent during the preceding fiscal year, including the average dollar amount repaid expressed as a percentage of the initial purchase price.

(7) If respondents choose to make a representation with respect to potential sales, income or gross or net profits such representation must be made only in the following manner:

(a) The number and percentage of franchisees which earned or made at least the same sales income or gross or net profits during a period of corresponding length in the immediate past as represented;

(b) The beginning and ending dates for the corresponding time period referred to in (a), above; and

(c) The following statement is clearly and conspicuously disclosed in immediate conjunction therewith, and in not less than ten (10) point boldface type:

THERE IS NO GUARANTEE THAT THESE [SALES] [INCOME] [AND/OR]

[PROFIT] PROJECTIONS WILL BE ACHIEVED BY YOU OR BY ANY SPECIFIC FRANCHISEE. THESE FIGURES ARE MERELY MANAGEMENT'S ESTIMATES OF THE [SALES] [INCOME] [PROFIT] THEY BELIEVE YOU MAY EXPECT FROM THE OPERATION OF THIS FRANCHISE BUSINESS. THERE IS THEREFORE AN ELEMENT OF RISK IN RELYING ON THESE ESTIMATES AS A BASIS FOR DETERMINING WHETHER YOUR DESIRE TO ENTER INTO A FRANCHISE RELATIONSHIP.

(8) All of the information, expressed in simple and readily understood language, as required by Paragraph I (F) of this order.

(9) If the respondents inform prospective franchisees that they intend to provide them with training or assistance, respondents disclose the specific details of such training or assistance to be provided.

(10) A verbatim copy of Paragraph IV (A) and (B) of this order.

(11) The name, address and telephone number of a person designated by respondents to whom franchise inquiries and complaints should be directed.

III

It is further ordered, That:

A. The following "NOTICE" be included immediately above and on the same page as the purchaser's signature line of any contract or agreement establishing or confirming a franchise and in boldface type no less than twelve (12) point type size:

"NOTICE"

(Non-Waiverable)

YOU MAY CANCEL THIS CONTRACT FOR ANY REASON WITHIN TEN (10) BUSINESS DAYS AFTER THE DAY YOU MAILED OR RETURNED THIS CONTRACT TO [COMPANY NAME], OR ITS OFFICER, AGENT, OR EMPLOYEE. **If you choose to cancel, you will be entitled to receive a full refund within ten (10) business days after [Company Name] receives notice of your cancellation. In order to cancel this contract and receive a full refund, send a letter which states your name and address and the fact that you cancel the contract. Send this letter by *Certified Mail, Return Receipt Requested* to:**

(Company Name)
(Street Name, Number)
(City, State, Zip Code)

B. Respondents shall not fail to cancel contracts and make refunds in accordance with the provisions contained in the "NOTICE" required by subparagraph (A), above.

IV

It is further ordered, That in all contracts, purchase agreements or any other binding obligation in connection with the sale or proposed sale of respondents' franchise, respondents shall clearly and conspicuously include therein the following provisions in at least eight (8) point type size and in the language specifically set forth as follows:

A. [Company Name] agrees to deliver or have delivered all merchandise, supplies and equipment; set up all business locations or retail store outlets; and take all other action as may be necessary to make your franchise fully operational within sixty (60) days from receipt of full payment, or cancel this contract and make refund of all money paid to [Company Name, officer, agent, or employee] within ten (10) business days thereafter.

B. If a business location or retail store outlet established by [Company Name] is terminated at the request of the owner, manager or operator of the said business location or retail store outlet within ninety (90) days from the date the business location or retail store outlet is fully operational and provided that purchaser has called at each said business location or retail store outlet for the purpose of taking inventory, replenishing the business location or retail store outlet with stock and making cash settlement at least once in each two week period since the business location or retail store outlet was fully operational, [Company Name] will, within five (5) business days from the day [Company Name] receives notice of said termination, notify the franchisee of its intention to:

(1) Provide, secure and set up a new business location or retail store outlet, by no later than twenty (20) business days after receiving the notice of termination; or

(2) Provide a refund, within twenty (20) business days from the day [Company Name] receives all of the photographic film and prepaid film processing envelopes remaining and unsold at the terminated business location or retail store outlet. The refund to be provided shall be computed as follows:

$$\frac{\text{The Number of Business Locations or Retail Store Outlets Terminated}}{\text{Total Number of Business Locations or Retail Store Outlets as Provided for in the Franchise Contract or Purchase Agreement}} \quad \text{X} \quad \text{Total Price Paid to [Company Name] for the Franchise} = \text{Refund}$$

C. Respondents shall not fail to cancel contracts, make refunds and provide new business locations or retail store outlets, in accordance with the provisions contained in subparagraph (A) and (B), above.

V

It is further ordered, That:

A. Respondents shall, within forty-five (45) days after the date this order becomes final, notify in writing, all past and present franchisees that any provision of respondents' contract or agreement which a franchisee is a party to, and which expressly limits the county or court in which they may institute a lawsuit against respondents, will not be enforced by respondents or used by respondents in defense of any lawsuit brought against respondents: Such written notification shall be made by *certified mail, return receipt requested,* to the last known address of all past and present franchisees. The return receipt for each notification mailed shall be maintained in respondents' files for a period not less than two (2) years from the day this order becomes final and such files shall be made available for inspection by the Commission or its representatives upon five (5) days written notice; and

B. Respondents shall not represent directly or by implication to any franchisee, nor raise in any lawsuit filed by a franchisee, that respondents and the franchisee have by contract or agreement limited the county or court in which a franchisee may institute a lawsuit.

VI

It is further ordered, That respondents shall maintain files, for a period of two (2) years, containing all complaints from prospective franchisees, and respondents' franchisees', and respondents' response thereto, and that such files be made available to employees of the Federal Trade Commission for inspection and copying upon five (5) days written notice.

VII

It is further ordered, That respondents:

A. Deliver a copy of this order to each present and future employee, agent, solicitor, independent contractor, or other person engaged by respondents in the promotion or sale of franchises, or who participate in the establishment of business locations or retail store outlets on behalf of respondents.

B. Obtain from each person identified in Paragraph VII (A), above, as a condition of their position or job, a signed written statement which provides the following: Name, residence address and telephone number and (1) acknowledgement of receipt of a copy of this order; and (2) an agreement to conform his/her practices to the requirements of this order; respondents shall retain such statements for a period of three (3) years subsequent to the termination of their position or job and make each statement available to the Commission's staff for inspection and copying upon five (5) days written notice.

C. Institute a program of continuing surveillance adequate to reveal whether each person described in subparagraph A of this paragraph is conforming to the requirements of this order.

D. Discontinue dealing with, or terminate the use or employment of, any person described in subparagraph (A), above, who refuses to sign a statement as described in subparagraph B of this paragraph, or who engages in any act or practice prohibited by this order.

VIII

It is further ordered, That respondents notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent such as dissolution, assignment, or sale resulting in the emergence of successor corporations, the creation or dissolution of subsidiaries, or any other change in the corporation which may affect compliance obligations arising out of this order.

IX

It is further ordered, That the individual respondent named herein promptly notify the Commission of the discontinuance of his present business or employment and of his affiliation with a new business or employment. In addition, for a period of ten years from the effective date of this order, the respondent shall promptly notify the Commission of each affiliation with a new business or employment. Each such notice shall include the respondent's new business address and a statement of the nature of the business or employment in which the respondent is newly engaged as well as a description of respondent's duties and responsibilities in connection with the business or employment. The expiration of the notice provision of this paragraph shall not affect any other obligation arising out of this order.

X

It is further ordered, That the respondents herein shall, within sixty (60) days after service upon them of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied with this order.

XI

It is further ordered, That in the event the Federal Trade Commission promulgates a Trade Regulation Rule applicable to respondents' business, this order shall be deemed modified to the extent it contravenes said Rule.

XII

It is further ordered, That respondents shall afford representatives of the Federal Trade Commission, upon five (5) days written notice, access to their records, memoranda, and other documents relating to the provisions contained herein, as may be appropriate to enable the Commission to determine respondents' compliance with this Agreement Containing Consent Order to Cease and Desist.

IN THE MATTER OF

TOWNSMAN-CENCO INTERNATIONAL, LTD., ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION AND WOOL PRODUCTS LABELING ACTS

Docket C-2920. Complaint, April 25, 1978 — Decision, April 25, 1978

This consent order, among other things, requires a New York City importer, manufacturer and distributor of clothing products to cease misrepresenting or failing to properly identify the wool and fiber content of their products.

Appearances

For the Commission: *Martin D. Gorman.*
For the respondents: *Pro se.*

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, as amended, and the Wool Products Labeling Act of 1939, and by virtue of the authority vested in it by said Acts, the Federal Trade Commission, having reason to believe that Townsman-Cenco International, Ltd., and Newcastle Imports, Ltd., corporations, and Seymour Hertling and George Center, individually and as officers of said corporations, hereinafter sometimes referred to as respondents, have violated the provisions of said Acts and the rules and regulations promulgated under the Wool Products Labeling Act of 1939, and it now appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent Townsman-Cenco International, Ltd. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York, with its office and principal place of business located at 105 Fifth Ave., New York, New York.

Respondent Newcastle Imports, Ltd. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York, with its office and principal place of business located at 276 Park Ave. South, New York, New York.

Respondents Seymour Hertling and George Center are officers of Townsman-Cenco International, Ltd. and Newcastle Imports, Ltd. They formulate, direct, and control the policies, acts and practices of the corporate respondents including those hereinafter set forth. Their office and principal place of business is the same as that of respondent Townsman-Cenco International, Ltd.

PAR. 2. Respondent Townsman-Cenco International, Ltd., is engaged in the business of manufacturing and distributing various products including wool blend men's suits. Respondent Townsman-Cenco International, Ltd. is also a wholesale distributor of men's clothing imported by respondent Newcastle Imports, Ltd.

Respondent Newcastle Imports, Ltd. is engaged in the importation of various products including wool blend men's slacks, distributed by respondent Townsman-Cenco International, Ltd.

PAR. 3. Respondents, now and for some time last past, have manufactured for introduction into commerce, imported for introduction into commerce, introduced into commerce, transported, distributed, delivered for shipment, shipped, offered for sale, and sold in commerce, as "commerce" is defined in the Wool Products Labeling Act of 1939, wool products as "wool product" is defined therein.

PAR. 4. Certain of said wool products were misbranded by the respondents within the intent and meaning of Section 4(a)(1) of the Wool Products Labeling Act of 1939 and the rules and regulations promulgated thereunder, in that they were falsely and deceptively stamped, tagged, labeled, or otherwise identified with respect to the character and amount of the constituent fibers contained therein.

Among such misbranded wool products, but not limited thereto, were certain wool blend men's suits and wool blend men's slacks, stamped, tagged, labeled or otherwise identified by respondents as "45% wool, 55% polyester" and as "40% wool, 60% polyester" whereas, in truth and in fact, said products contained substantially different fibers and amounts of fibers than represented.

PAR. 5. Certain of said wool products were further misbranded by respondents in that they were not stamped, tagged, labeled, or otherwise identified as required under the provisions of Section 4(a)(2) of the Wool Products Labeling Act of 1939 and in the manner and form as prescribed by the rules and regulations promulgated under said Act.

Among such misbranded wool products, but not limited thereto, were wool products, namely wool blend men's suits and slacks, with labels on or affixed thereto, which failed to disclose the percentage of the total fiber weight of the said wool products, exclusive of ornamentation not exceeding 5 per centum of said total fiber weight, of (1) wool, (2) reprocessed wool, (3) reused wool, (4) each fiber other than wool, when said percentage by weight of such fiber was 5 per centum or more, and (5) the aggregate of all other fibers.

PAR. 6. The acts and practices of respondents as set forth in Paragraphs Four and Five were, and are, in violation of the Wool Products Labeling Act of 1939 and the rules and regulations promulgated thereunder, and constituted, and now constitute, unfair methods of competition and unfair and deceptive acts and practices, in or affecting commerce, under the Federal Trade Commission Act, as amended.

PAR. 7. Respondents are now and for some time past have been engaged in the importation, offering for sale, sale, and distribution of certain products, namely men's suits and slacks. In the course and conduct of their business as aforesaid, respondents now cause and for some time last past, have caused their said products, when sold, to be shipped from their places of business in the State of New York to purchasers located in various other States of the United States, and maintain and at all times mentioned herein have maintained, a substantial course of trade in said products in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended.

PAR. 8. Respondents in the course and conduct of their business have made statements on invoices to their customers misrepresenting the fiber content of certain of their products.

Among such misrepresentations, but not limited thereto, were statements setting forth the fiber content thereof as "55% polyester, 45% wool," "60% polyester, 40% wool" whereas, in truth and in fact, said products contained substantially different fibers and amounts of fibers than represented.

PAR. 9. The acts and practices set out in Paragraph Eight have the tendency and capacity to mislead and deceive the purchasers of said products as to the true content thereof.

PAR. 10. The aforesaid acts and practices of the respondents as herein alleged in Paragraph Eight were, and are, all to the prejudice and injury of the public, and constituted, and now constitute, unfair and deceptive acts or practices in or affecting commerce, within the intent and meaning of the Federal Trade Commission Act, as amended.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondents named in the caption hereof, and the respondents having been furnished thereafter with a copy of a draft of complaint which the New York Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with violation of the Federal Trade Commission Act, as amended, and the Wool Products Labeling Act of 1939; and,

The respondents and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and,

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondents have violated the said Acts, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent Townsman-Cenco International, Ltd. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York, with its office and principal place of business located at 105 Fifth Ave., New York, New York.

Respondent Newcastle Imports, Ltd. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York, with its office and principal place of business located at 276 Park Ave. South, New York, New York.

Respondents Seymour Hertling and George Center are officers of said corporations. They formulate, direct and control the policies, acts and practices of said corporations, and their address is 105 Fifth Ave., New York, New York.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents and the proceeding is in the public interest.

ORDER

It is ordered, That respondents Townsman-Cenco International, Ltd., a corporation, Newcastle Imports, Ltd., a corporation, their successors and assigns, and their officers, and Seymour Hertling and George Center, individually and as officers of said corporations, and respondents' representatives, agents and employees, directly or through any corporation, subsidiary, division or any other device, in connection with the introduction, or importing for introduction, into commerce, or the offering for sale, sale, transportation, distribution, delivery for shipment or shipment, in commerce, of wool products, as "commerce" and "wool product" are defined in the Wool Products Labeling Act of 1939, do forthwith cease and desist from misbranding such products by:

1. Falsely and deceptively stamping, tagging, labeling or otherwise identifying such products.

2. Failing to securely affix to or place on each such product a stamp, tag, label or other means of identification showing in a clear and conspicuous manner each element of information required to be disclosed by Section 4(a)(2) of the Wool Products Labeling Act of 1939.

It is further ordered, That respondents Townsman-Cenco International, Ltd., a corporation, Newcastle Imports, Ltd., a corporation, their successors and assigns, and their officers, and Seymour Hertling and George Center, individually and as officers of said corporations, and respondents' representatives, agents and employees, directly or through any corporate or other device, in connection with the importing, advertising, offering for sale, sale or distribution of clothing in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, do forthwith cease and desist from misrepresenting such products on invoices or shipping memoranda applicable thereto, or in any other manner.

It is further ordered, That respondents mail a copy of this order by registered mail to each of their customers that purchased the wool products described in this complaint.

It is further ordered, That the respondent corporations shall forthwith distribute a copy of this order to each of their operating divisions.

It is further ordered, That respondents notify the Commission at least 30 days prior to any proposed change in the corporate respondents such as dissolution, assignment or sale resulting in the emergence of successor corporations, the creation or dissolution of subsidiaries or any other change in the corporations which may affect compliance obligations arising out of the order.

It is further ordered, That each individual respondent named herein promptly notify the Commission of the discontinuance of his present business or employment and of his affiliation with a new business or employment. In addition, for a period of ten years from the effective date of this order, each respondent shall promptly notify the Commission of each affiliation with a new business or employment. Each such notice shall include the respondent's new business address and a statement of the nature of the business or employment in which the respondent is newly engaged as well as a description of respondents' duties and responsibilities in connection with the business or employment. The expiration of the notice provision of this paragraph shall not affect any other obligation arising under this order.

It is further ordered, That the respondents herein shall within sixty

(60) days after service upon them of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied with this order.

IN THE MATTER OF

JAY NORRIS CORP., ET AL.

ORDER, OPINION, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket 9054. Complaint, Sept. 3, 1975—Final Order, May 2, 1978

This order, among other things, requires a Freeport, L.I., N.Y. mail-order house to cease misrepresenting, in the advertising and sale of consumer products, that dissatisfied customers will receive prompt refunds; and that exchanges and refunds are expeditiously processed; that all parcels are insured against loss or damage; and that non-delivery is caused by the United States Postal Service. The order requires that purchases be shipped within time periods specified, and in the event of shipping delays, customers must be offered the option of consenting to the delays or cancelling their transactions. The firm is further obligated to honor such cancellations and to make proper refunds in a timely manner. The order further prohibits the company from making false or unsubstantiated claims regarding the characteristics, efficacy, performance, safety, and value of its consumer products. Additionally, the order requires the corporation and the Pan-Am Car Distributors Corp., both engaged in the advertising and sale of used motor vehicles, to cease misrepresenting that their vehicles have been inspected and repaired in preparation for delivery to purchasers; or that they are in a safe mechanical and operation condition and will render normal, adequate and satisfactory service.

Allegations of the complaint are dismissed as to Federated Nationwide Wholesalers Service, Garydean Corp., t/a Nationwide Wholesalers Service, and P-N Publishing Company, Inc.

Appearances

For the Commission: *Irving C. Koch* and *Sol Grand.*

For the respondent: *Robert Ullman, Bass, Ullman & Lustigman,* New York City.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Jay Norris Corp., Federated Nationwide Wholesalers Service, Garydean Corp., a corporation trading as Nationwide Wholesalers Service, P–N Publishing Company, Inc., a corporation, Pan-Am Car Distributors Corp., a corporation and Joel Jacobs, Mortimer Williams and Kenneth Mann, individually and as officers of said corporations, hereinafter referred to as the respondents, have violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint, stating its charges in that respect as follows:

I. RESPONDENTS

PARAGRAPH 1. Respondents Jay Norris Corp., Federated Nationwide Wholesalers Service, Garydean Corp., trading as Nationwide Wholesalers Service, [2] P-N Publishing Company, Inc., and Pan-Am Car Distributors Corp. are corporations organized, existing and doing business under and by virtue of the laws of the State of New York, with their principal offices and place of business located at 31 Hanse Ave., Freeport, Long Island, New York.

Individual respondents Joel Jacobs and Mortimer Williams are officers of said corporations. Kenneth Mann is an officer of Pan-Am Car Distributors Corp. They formulate, direct and control the acts and practices of the corporate respondents including the acts and practices hereinafter set forth. Their business addresses are the same as that of the corporate respondents.

II. NATURE OF RESPONDENTS' BUSINESS

PAR. 2. Respondents are engaged in the advertising, offering for sale, sale and distribution of numerous articles of merchandise by mail order which they offer through newspaper, magazine, and catalog advertisements, including roach powder, TV antennas, socks, flashlights, flame guns, jewelry, books, girdles, watches, home furnishings, cheeses, ex-taxis sold as used cars and numerous other articles of merchandise.

PAR. 3. Respondents in the course and conduct of their business have been and are now engaged in the advertising, offering for sale, sale and distribution of merchandise which they ship or cause to be shipped when sold, from the State of New York to purchasers located in various other States of the United States or directly from manufacturers and distributors located in various other States to purchasers located throughout the nation, and have maintained a substantial course of trade in said merchandise in or affecting commerce as "commerce" is defined in the Federal Trade Commission Act.

PAR. 4. Respondents are now, and at all times mentioned herein have been, in substantial competition in commerce with other corporations, [3] firms and individuals engaged in the sale and distribution of products of the same general kind and nature as those sold by respondents.

III. ACTS AND PRACTICES – REPRESENTATIONS

PAR. 5. In the course and conduct of their business, and for the purpose of inducing the purchase of their products, respondents have made statements and representations in the advertising, offering for sale, sale and distribution of their products through flyers, catalogs, brochures and advertisements published in mail order catalogs and national newspapers and magazines.

PAR. 6. The statements and representations made as alleged in Paragraph Five hereof, include statements regarding respondent's guarantees, deliveries and refunds. Typical and illustrative, but not all inclusive, of statements and representations with respect to their guarantees, deliveries and refunds, are the following:

30-DAY MONEY-BACK GUARANTEE Mail No-Risk Coupon Now

ORDER BY MAIL WITH CONFIDENCE 30-DAY MONEY-BACK GUARANTEE

30-DAY MONEY-BACK GUARANTEE ON ALL PURCHASES

30-DAY MONEY-BACK GUARANTEE ON ALL PURCHASES CHRISTMAS DELIVERY GUARANTEED IF YOU ORDER NOW

BUY WITH CONFIDENCE! If not delighted, return your order within 30 days for refund of full purchase price

MONEY-BACK IF NOT DELIGHTED-SEND CHECK OR MONEY ORDER

ORDER NOW PROMPT DELIVERY GUARANTEED

"PERSONAL CHECKS" To insure immediate shipment of your order, please have your check certified. [4] Otherwise, allow about 2 weeks until your check clears your bank

Satisfaction quaranteed or money refunded

YOUR GUARANTEE OF SATISFACTION. . .Everything you buy from JAY NORRIS CORP. is ALWAYS FIRST QUALITY. Any item not up to your expectations return in 30 days for full refund.

Unless item is marked express collect, use this easy chart to figure postage insurance, shipping and handling charges. It's only part of the delivery cost-we pay the rest.

-If Your Order Is- up to

$15.00	add $1.70
$15.01 to $20.00	add $2.20
$20.01 to $30.00	add $3.20
$30.01 to $40.00	add $4.20
$40.01 to $50.00	add $5.20
$50.01 to $60.00	add $6.00
over $60.00	add $7.20

DIRECT FACTORY SHIPMENT:
Some items in this catalog are shipped direct from the factory. Such shipments are sent to you Parcel Post, Express Collect or Freight Collect, depending on weights

REFUND: If for any reason, there is a refund due you after your order has been filled, we will send you such refund promptly.

SHIPPING INFORMATION:
Orders are usually filled within 24 hours of receipt (with the exception of factory shipments). . .Allow 1 to 3 weeks for factory shipments to reach you . . .

Dear Customer:

Because you did not receive your order, we must assume that it was lost in the mails. [5]

If you will be kind enough and return all these papers together with the original or photostatic copy of your check or money order, showing that it was cashed by us, a tracer will be placed and if necessary, a duplicate shipment will be made.

Please give us full details and information pertaining to the merchandise, such as size, color, price, style number, etc.

We regret any inconvenience we may have caused you. Thank you for your cooperation.

Very truly yours,
JAY NORRIS CORP.

PAR. 7. Through the use of the statements and representations alleged in Paragraph Six hereof, and others of similar import and meaning, respondents have represented, and are now representing, directly or by implication, that:

1. Merchandise paid for by a certified check is shipped to purchasers immediately.

2. Merchandise paid for by a non-certified check is shipped to purchasers about two weeks after said check has been approved for payment at the purchaser's bank.

3. The full purchase price of the product plus all additional charges paid by the purchaser in connection with said purchase are refunded by respondents if the purchaser is dissatisfied for any reason.

4. A sum of money in the form of cash, check, money order or other negotiable currency is refunded to purchasers if they are dissatisfied for any reason.

5. Pursuant to respondents' 30-day money back guarantee, purchasers will receive a full refund if the merchandise is returned to respondents within 30 days from the date of the purchaser's receipt of said merchandise. [6]

6. In a substantial number of cases, the non-delivery of the

purchaser's order, is caused by the loss of the merchandise by the United States Postal Service.

7. Purchasers of respondents' products pay only part of the delivery cost and the respondents absorb the remaining portion of said cost.

8. Exchanges or refunds are expeditiously processed by respondents.

9. All parcels shipped to purchasers, except those items marked express collect, are insured against loss, damage or other casualty by respondents.

PAR. 8. In truth and in fact:

1. In numerous instances, merchandise paid for by a certified check is not shipped to purchasers immediately. Delays of as long as one month to one year have been encountered.

2. In numerous instances, merchandise paid for by a non-certified check is not shipped to purchasers about two weeks after said check has been approved for payment at the purchaser's bank. Delays of as long as one month to one year have been encountered.

3. The full purchase price of the product, plus all additional charges paid by the purchaser in connection with said purchase, are not refunded by respondents if the purchaser is dissatisfied. Postage, handling, shipping and insurance claims are deducted by respondents from the full purchase price.

4. A sum of money in the form of cash, check, money order or other negotiable currency is not refunded to purchasers if they are dissatisfied for any reason. Respondents [7] give purchasers a credit certificate which must be used to purchase merchandise from the respondents or be returned to the respondents in order to receive a cash refund.

5. Pursuant to respondents' 30-day money back guarantee purchasers do not receive a full refund if the merchandise is returned to respondents within 30 days from the date of the purchaser's receipt of said merchandise.

6. In numerous instances, the non-delivery of the purchaser's order is not caused by the loss of the merchandise by the United States Postal Service. Rather, respondents have failed to ship the ordered merchandise.

7. In numerous instances, the respondents do not absorb a portion of the delivery cost. Purchasers of respondents' merchandise pay the full cost of delivery.

8. In numerous instances, exchanges or refunds are not expeditiously processed by respondents. Delays of many months have been

encountered and only after purchasers write to the respondents and to governmental authorities are refunds received.

9. All parcels shipped to purchasers except those items marked express collect, are not insured against loss, damage or other casualty by respondents.

Therefore, the statements and representations, alleged in Paragraph Six hereof, were, and are, unfair or deceptive.

PAR. 9. The statements and representations made as alleged in Paragraph Five hereof include statements and representations regarding the performance, efficacy and other characteristics of respondents' products. Typical and illustrative, [8] but not all-inclusive, of the statements and representations with respect to product performance, efficacy and other characteristics are the following:

FLAME GUN

NEW JN INSTA-JET PROPANE FLAME GUN THE WORK-SAVER THE HEART-SAVER LIGHTWEIGHT, EASY-HANDLING FASTEST WAY WE KNOW TO CLEAR AWAY ICE AND SNOW! . . . Whips through even the heaviest drifts. Clears walks and driveways. Routs Clogged gutters of ice and old leaves.

Thaws frozen pipes . . . . Produces a clean hot flame for up to 14 hours on a single propane cylinder-easily obtainable at hardware, paint and department stores . . .

Just aim The Flame Gun and watch it dissolve the heaviest snow drifts, whip right through the thickest ice . . . in seconds!

SOCKS

YOU'LL NEVER NEED TO BUY ANOTHER PAIR OF SOCKS AGAIN FOR THE REST OF YOUR LIFE. (unless your laundry loses them) . . . IMMEDIATE DELIVERY GUARANTEED

. . . indestructible nylon socks . . .

. . . Guaranteed to wear forever in normal use - that "normal use" simply means don't burn holes in them deliberately, or try to cut them with scissors or razor . . .

These revolutionary 8-ply nylon socks are made of yarn so indestructible we unconditionally guarantee to give you FREE replacement pair for pair - for any you ever wear a hole in! 6 pair only $7.98 12 pair for $14.98 [9]

ROACH POWDER

Get rid of roaches ONCE AND FOR ALL! SURE-KILL WIPES OUT ROACH NESTS OR YOU PAY NOTHING Roaches can't resist Sure-Kill. They devour its odorless white powder and crawl to their nests, where they die. Then, a deadly chain reaction starts, that wipes out every roach and every egg in the nest. Sure-Kill is safe to use, and never loses its killing power-even after years. A single can cleans out 6 to 8 rooms

GUARANTEED ROACH-FREE FOR 5 YEARS. Sure-Kill roach killer is guaranteed by the manufacturer to prevent reinfestation for up to 5 years when used as directed and left in place.

UNCONDITIONAL GUARANTEE Our roach killer is guaranteed by the manufacturer to prevent reinfestation when used as directed and left in place or your money back

. . . Completely safe to use, and never loses its killing power-even after years. . .

TV ANTENNA

ELECTRONIC MIRACLE TURNS YOUR HOUSE WIRING INTO JUMBO TV ANTENNA. . .ONLY $1.99 - 2 for $3.65 now you can bring in every channel in your area sharp and clear without installing an expensive outdoor antenna or using unsightly rabbit ears. This simple little invention does the trick. You attach it easily and quickly to your TV set, then plug it into wall outlet. . .makes your home wiring a huge antenna for super reception . . .

Every home a super receiver ELECTRONIC MIRACLE [10] TURNS YOUR HOUSE WIRING INTO A JUMBO TV ANTENNA. . . .

. . .Do you know that you have one of the greatest TV antennas ever constructed? It's better than any set of rabbit ears, more efficient than complicated external antennas. It's your house. Yes, the wiring in your home constitutes a great antenna that acts as a super receiver for TV, FM, all kinds of difficult reception. . . .

FLASHLIGHT

NEW! 5 - YEAR FLASHLIGHT USED ON THE APOLLO MISSIONS DEVELOPED FOR AMERICA'S ASTRONAUTS Totally new and revolutionary power cell (developed and used by the government in manned moon flights) keeps this flashlight shining bright for at least 5 years with 10 times the staying power of an ordinary flashlight. No external switch to corrode or break. (NASA wanted a fool-proof switch for their flashlight going to the moon). Now you can have it for your car or home - YOUR COST $7.99, 2 for $14.99

ABSOLUTE 5 - YEAR GUARANTEE Every command modual flashlight carries this absolute 5 - year guarantee. Carry your flashlight with you, keep it at home. It must work even if you haven't touched it for 5 years or your money back. So don't be another minute without the one safety element every car, every family needs.

CARS

BUY CHOICE . . . NOT CHANCE Buy direct and get the carefully maintained car of your choice below wholesale price. All cars are standard four door, six passenger sedans equipped with automatic transmissions, heater, defroster and feature durable vinyl interiors. They have been in regularly maintained fleet use and serviced far more frequently than the average car owner can afford to do. Each car has been thoroughly serviced by our mechanics [11] to put it in good operating condition and passes careful inspection before being released for delivery. These top-quality ex-taxis have been carefully selected for best value . . . We offer these fine cars at the prices shown (F.O.B., N.Y.) There are no hidden costs. . . .

IDEAL FOR PERSONAL USE OR TO RESELL AT A PROFIT!

1970 DODGE CORONET, AUTOMATIC TRANSMISSION $999.

1969 FORD CUSTOM DODGE CORONET, AUTOMATIC TRANSMISSION $799.

1969 CHEVROLET BISCAYNE, AUTOMATIC TRANSMISSION, $899.

Only Pan Am gives you this 100% o.k. checkout certificate. Dependable Pan Am gives you a good car at a low price. Our highly trained mechanics double-check each car for all the terms below. When a car leaves our premises it is checked out as follows:

Brakes
Plugs
Points
Lights
Battery
Generator
Fan Belt
Spare Tire
Jack
Transmission
Heater
Defroster
Starter
Water Pump
Fuel Pump
Block
Color

MAIL THIS COUPON WITH YOUR DEPOSIT – ORDER AS MANY AS YOU WANT. ALL CARS ARE SOLD ON AN AS IS FIRST ORDER FIRST SERVE BASIS.

LINCOLN – KENNEDY PENNY

NOW AVAILABLE THE ONLY LINCOLN-KENNEDY PENNY EVER MINTED UNCIRCULATED COMMEMORATIVE LINCOLN HEAD PENNY WITH KENNEDY PROFILE Here's unusual news for collectors and anyone interested in unique commemorative issues. . .issues that may never be repeated again. A new uncirculated Lincoln Head penny is now available. This [12] unique coin shows the profile of President Kennedy stamped on the surface looking at President Lincoln. The relationship is uncanny. Never released for ordinary use, the coin is perfectly legal tender and is sanctioned by Section 332 of the U.S. Code. As a coin of both historical and numismatic significance it is certain to become a collector's item that will grow and grow in value. Because, however, this coin is not in circulation, you may obtain it only through an offering of this sort, and we urge you to order now, avoid disappointment. And if you order right away, you will also receive the Plaque of Coincidences showing the startling parallels in the career of these two tragic figures. . . .

. . . These and many more astonishing coincidences are yours in your Free Plaque of Coincidential Facts when you order The Lincoln-Kennedy Commemorative Penny.

PAR. 10. Through the use of the statements and representations alleged in Paragraph Nine hereof, and others of similar import and meaning, respondents have represented and are now representing, directly or by implication that:

FLAME GUN

1. The "JN INSTA-JET PROPANE FLAME GUN" is able to whip through

the heaviest snow drifts and the thickest ice in seconds and is effective and efficient in clearing walks and driveways of ice and snow.

SOCKS

2. Respondents' nylon socks are indestructible.
3. Respondents' nylon socks last forever.

ROACH POWDER

4. Respondents' roach powder is safe to use.
5. Respondents' roach powder gets rid of roaches once and for all.

[13]

6. Respondents' roach powder creates a deadly chain reaction which eliminates and kills roaches and eggs.
7. The manufacturer has unconditionally guaranteed that respondents' roach powder prevents reinfestation when used as directed and left in place or it will refund money.
8. Respondents' roach powder does not lose its capacity to kill under any conditions of use.

TV ANTENNA

9. Respondents' TV antenna will bring sharp and clear reception even in difficult areas.
10. The performance of respondents' TV antenna is superior to any rabbit ear antenna or outdoor antenna.
11. Respondents' TV antenna will turn all types of house wiring into a TV antenna.
12. Respondents' TV antenna is an electronic miracle.

FLASHLIGHT

13. Respondents' "FIVE YEAR FLASHLIGHT" carries an absolute 5-year guarantee.

CARS

14. Cars delivered to purchasers are in good mechanical and physical condition.
15. Cars delivered to purchasers are in safe operating condition.
16. Cars delivered to purchasers are finished and look as pictured and described in respondents' advertising materials. [14]
17. Cars are checked by expert mechanics and necessary repairs are made prior to release for delivery.

18. Cars delivered to purchasers are in sound condition and repair and render normal, adequate and satisfactory service.

19. Respondents' cars may be readily resold by the purchasers at a profit.

20. Cars are regularly ordered and received in advance of their being offered for sale and are held in stock until purchase orders are received.

21. Respondents' cars have undergone thorough and complete servicing and inspection before being released and approved for delivery.

22. Each price quoted for respondents' motor vehicles is the full price and there are no hidden costs.

23. Respondents bear the liability and responsibility of delivery of cars to purchasers at any destination in the United States where such purchasers may reside.

LINCOLN-KENNEDY PENNY

24. Respondents' Lincoln-Kennedy penny was minted by the United States Treasury Department.

25. Respondents' Lincoln-Kennedy penny is a coin of historical and numismatic significance which is certain to grow in value.

26. The issuance of respondents' Lincoln-Kennedy penny was sanctioned by Section 332, Title 18, U.S. Code.

27. A free plaque containing historical coincidences between the lives of President Lincoln and President Kennedy is provided to purchasers with each coin order. [15]

PAR. 11. In truth and in fact:

FLAME GUN

1. The "JN INSTA-JET PROPANE FLAME GUN" is not able to whip through the heaviest snow drifts and the thickest ice in seconds and is not effective and efficient in clearing walks and driveways of ice and snow.

SOCKS

2. Respondents' nylon socks are not indestructible.

3. Respondents' nylon socks do not last forever.

ROACH POWDER

4. Respondents' roach powder is not safe to use. Ingestion of the powder may cause sickness or death.

5. Respondents' roach powder does not get rid of roaches once

and for all. The roach powder is a formulation of boric acid which works slowly. In many residential buildings cockroaches can reinfest before they are eliminated.

6. Respondents' roach powder does not create a deadly chain reaction which eliminates and kills roach and eggs. Each cockroach must contact the insecticide to be killed. Respondents' roach powder will not kill roach eggs.

7. The manufacturer has not unconditionally guaranteed that respondents' roach powder prevents reinfestation when used as directed and left in place or it will refund money.

8. Respondents' roach powder loses its capacity to kill under certain conditions of use. If wet, it cakes and does not adhere to the insects. If covered by grease or food deposits or non-insecticidal dusts, it becomes ineffective. [16]

TV ANTENNA

9. Respondents' TV antenna will not bring sharp and clear reception in difficult areas.

10. The performance of respondents' TV antenna is not superior to rabbit ear antennas or to outdoor antennas.

11. Respondents' TV antenna will not turn all types of house wiring into a TV antenna. If house wiring is encased in metal, it is shielded from the reception of any TV signals.

12. Respondents' TV antenna is not an electronic miracle.

FLASHLIGHT

13. Respondents' "FIVE YEAR FLASHLIGHT" does not carry an absolute 5-year guarantee. The flashlight is guaranteed by the manufacturer to store and remain usable for 5 years or to operate for a total of 10 hours, which ever comes first. The manufacturer further clearly states in its guarantee that the light will not stay "on" continuously for 5 years.

CARS

14. In a number of instances, cars delivered to purchasers are not in good mechanical and physical condition.

15. In a number of instances, cars delivered to purchasers are not in safe operating condition.

16. In a number of instances, cars delivered to purchasers are not finished and do not look as pictured and described in respondents' advertising materials. [17]

17. In a number of instances, cars are not checked by expert

mechanics and necessary repairs are not made prior to release for delivery.

18. Cars delivered to purchasers are not in sound condition and repair and do not render normal, adequate and satisfactory service.

19. Respondents' cars may not be readily resold by the purchasers at a profit.

20. In a number of instances, cars are not regularly ordered and received in advance of their being offered for sale and are not held in stock until purchase orders are received.

21. In a number of instances, respondents' cars have not undergone thorough and complete servicing and inspection before being released and approved for delivery.

22. In numerous instances, each price quoted for respondents' motor vehicles is not the full price and there are hidden costs. Purchasers are often required to expend large sums of money for the delivery of the cars or to enable cars to pass state motor vehicle registration safety or inspection requirements or to put cars into safe operating condition.

23. Respondents do not bear the liability or responsibility for delivery of cars to purchasers at any destination in the United States where such purchasers may reside.

LINCOLN-KENNEDY PENNY

24. Respondents' Lincoln-Kennedy penny was not minted by the United States Treasury Department. No branch of the United States Government had anything to do with the production of this coin. [18]

25. Respondents' Lincoln-Kennedy penny is not a coin of historical and numismatic significance which is certain to grow in value. It is a privately produced novelty item using an ordinary penny.

26. The issuance of respondents' Lincoln-Kennedy penny was not sanctioned by Section 332, Title 18, U.S. Code. Section 332 refers to the debasement of gold and silver coins by the physical removal or dimunition of the gold or silver content.

27. A free plaque containing historical coincidences between the lives of President Lincoln and President Kennedy is not provided to purchasers with each coin order. The ordinary paper card upon which the Lincoln-Kennedy penny is pasted is neither "free" nor is it a "plaque." Said card was never offered for sale by respondents at a regular price but was always offered for sale in conjunction with the penny.

Therefore, the statements and representations as alleged in Paragraph Nine hereof were, and are, unfair or deceptive.

IV. ACTS OR PRACTICES – FAILURE TO DISCLOSE MATERIAL FACTS

PAR. 12. In the further course and conduct of their business, as aforesaid, respondents have made statements and representations as aforesaid, without disclosing material facts. Such material facts include, but are not limited to, the following:

FLAME GUN

Initial purchase of respondents' flame gun does not include the propane cylinder mentioned in respondents' advertisements of its flame gun. The propane cylinder, which is an essential component of the flame gun, must be purchased at an additional cost. [19]

Respondents' flame gun is not assembled when delivered but rather must be assembled by purchasers after delivery.

ROACH POWDER

Respondents' roach powder is 50% boric acid and 50% inert ingredients.

Respondents' roach powder is hazardous. The product may be harmful to human beings and pets. Special precautions should be taken in the use of this product.

FLASHLIGHT

Respondents' flashlight has an on life of 10 to 20 hours.

Manufacturer's guarantee of respondents' flashlight is not absolute. The manufacturer guarantees that the light can be stored and remain usable for 5 years or operate for a total of ten hours, whichever comes first.

CARS

Respondents' cars are ex-New York City taxicabs.

Respondents' advertise that the cars are "FOB New York" and "As Is" without disclosing the import or meaning of those terms.

Respondents' cars are not inspected for compliance with any state motor vehicle inspection law.

Interiors of motor vehicles have not been cleaned or reconditioned by respondents prior to their being offered for sale.

Drivers hired to deliver cars to purchasers are independent contractors and are not respondents' agents, servants or employees.

The aforesaid material facts, if known to consumers would be likely to affect their consideration of whether or not to purchase respondents' products. Therefore, the advertisements, acts or practices, which fail to disclose the aforesaid material facts are unfair or deceptive. [20]

V. OTHER ACTS AND PRACTICES

PAR. 13. In the further course and conduct of their business as aforesaid respondents have:

(a) Deposited purchasers' checks and money orders into their bank accounts within three days to one week from receipt of such checks and money orders and have failed to either ship the merchandise ordered or to refund money for one month to one year;

(b) Failed to answer letters of inquiry from consumers or have made inadequate responses which have thereby delayed or prevented purchasers, seeking deliveries of merchandise or refunds of their money, from obtaining same;

(c) Failed to provide a business telephone listing in the official telephone directory for its location or in any published telephone directory and have maintained an unlisted business telephone number;

(d) Placed the burden of record keeping upon the purchasers who, upon seeking a refund, exchange, or delivery of the advertised merchandise ordered and paid for by them, have been required by respondents to provide copies of their cancelled checks, original order blanks or various correspondence received from respondents, as well as the full details pertaining to the merchandise ordered such as the size, color, price, style number and the date the order was placed;

(e) Utilized numerous corporate and business names such as Jay Norris Corporation, P.N. Publishing Corporation, Norris Nutrition, Garydean Corp., Federated Nationwide Wholesalers Service, Federated Wholesalers Service, Nationwide Service, Cheese[21]lovers International, Pan American Car Distributors Corporation, Associated Auto Wholesalers Corporation, American Value Corporation, and various other corporate and business names, post office box numbers and addresses, in such manner as to create confusion in the minds of purchasers who are unable to relate all the names used to the Jay Norris Corporation or to its principal owners.

Such business practices by respondents constitute unfair or deceptive acts or practices and unfair methods of competition in commerce in violation of Section 5 of the Federal Trade Commission Act.

PAR. 15. The use by respondents of the aforesaid unfair or deceptive representations, acts and practices has had, and now has, the capacity and tendency to mislead members of the purchasing public into the erroneous and mistaken belief that said statements and representations were and are true and into the purchase of a substantial volume of respondents' products.

PAR. 16. The aforesaid acts and practices of respondents as herein alleged are all to the prejudice and injury of the public and of respondents' competitors, constitute unfair methods of competition in or affecting commerce and unfair or deceptive acts or practices in violation of Section 5 of the Federal Trade Commission Act.

INITIAL DECISION BY MILES J. BROWN, ADMINISTRATIVE LAW JUDGE

AUGUST 31, 1977

PRELIMINARY STATEMENT

The Federal Trade Commission issued its complaint in this matter on September 3, 1975 (mailed October 3, 1975), charging respondents with unfair methods of competition in or affecting commerce and unfair or deceptive acts or practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act, as amended, (15 U.S.C. 45). [2]

In their answer, respondents denied that they had violated the Federal Trade Commission Act as alleged in the complaint. They asserted that the individual respondents acted only in their capacity as corporate officers. They further asserted that the respondent corporations, other than J. Norris Corp. ("Norris") and Pan-Am Car Distributors Corp. ("Pan-Am"), had nothing to do with the matters which were the subject of the complaint.

Thereafter, for approximately ten months, there was sporadic pretrial discovery occasioned by several long continuances prompted by the fact that the complaint counsel originally assigned to this matter was concurrently handling another adjudicative matter on which she was the only Federal Trade Commission counsel of record. On July 6, 1976, complaint counsel filed a list of witnesses containing 140 names. On August 2, 1976, complaint counsel filed her 219 page list of Commission exhibits identifying 4236 numbered documents (many multi-paged) and not cross-referenced to the allegations of the complaint. Whereupon respondents' counsel moved for an extension of time until December 30, 1976, in which to file their witness and document lists, on the grounds that the "overwhelming volume of complaint counsel's avalanche of documents (not to mention the list of 140 witnesses) represents extraordinary cause for this request." (Motion for Rescheduling of Dates . . ., dated August 17, 1976.)

On September 9, 1976, the administrative law judge issued an order requiring complaint counsel to file amended lists of proposed exhibits and proposed witnesses and otherwise vacated all other pretrial requirements therefore imposed on counsel. Shortly thereafter, other complaint counsel were assigned to this matter. On November 30, 1976, substitute complaint counsel filed their amended and abbreviated lists.

Adjudicative hearings commenced on January 11, 1977. Complaint counsel concluded their case-in-chief on February 1, 1977, utilizing 14 trial days. Respondents' answering case commenced February 28, 1977. On March 2, 1977, after three days of hearings, respondents' counsel advised that respondent Joel Jacobs, the only remaining witness for respondents, was incapaciated and he requested a continuance of the hearings. After several hearing dates were postponed, due to the continuing incapacity of Mr. Jacobs, the parties, on April 21, 1977, filed a stipulation consenting to the written testimony of Joel Jacobs, including questions and answers on direct examination, as well as on cross-examination. On April 28, 1977, [3] the administrative law judge approved the stipulation and directed that Mr. Jacob's written testimony be incorporated into the record.

On May 23, 1977, the administrative law judge was notified that the exhibits, which had remained in the New York Regional Office since the last hearing date of March 2, 1977, pending further hearings for presentation of Mr. Jacob's testimony, had been delivered to the Secretary's office. On June 1, 1977, the administrative law judge issued his order making certain corrections to the record, closing the record for receipt of evidence, and establishing due dates for filing of proposed findings and reply briefs.[1]

Any motions appearing on the record not heretofore or hereby specifically ruled upon either directly or by the necessary effect of the conclusions in this initial decision are hereby denied.

The proposed findings and conclusions submitted by counsel supporting the complaint ("CSCPF") and counsel for respondents ("Resp. PF") have been given careful consideration and to the extent not adopted by this decision, in the form proposed or in substance, are rejected as not supported by the evidence or as immaterial.

This case deals with certain matters relating to the business of selling, by mail-order, through advertisements disseminated by catalogs and newspapers or magazines. Certain challenged acts and practices relate to the handling of orders and shipments and, in addition, to respondents' handling of consumers' inquiries and complaints relative to non-delivery, money-back guarantees and refunds. Other matters relate to certain advertising representations concerning the efficacy, performance and characteristics of specific products and the truth or falsity of such representations. Allegations relating to the failure to disclose material facts were also included in the complaint.

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[1] On August 16, 1977, the administrative law judge requested an extension of time until September 13, 1977, in which to file this initial decision. On August 30, 1977, he was notified that the Commission had granted his request.

Having reviewed the entire record in this proceeding, and having considered the demeanor of the witnesses[2] [4] together with the pleadings, the proposed findings, conclusions, and arguments submitted by counsel supporting the complaint and counsel for respondents, I make the following findings of fact based on the record considered as a whole:

FINDINGS AS TO THE FACTS

About the respondents.

1. Respondents Norris, Pan-Am, Federated Nationwide Wholesalers - Garydean Corp.[3] ("Federated") and P-N Publishing Company, Inc. ("P-N") are all New York corporations with their principal offices located at 31 Hanse Ave., Freeport, Long Island, New York (Compl. Par. 1; Ans. Par. 1).

2. Respondents Joel Jacobs ("Jacobs") and Mortimer Williams ("Williams") are the sole shareholders, officers and directors of Norris, Federated and P-N (Compl. Par. 1; Ans. Par. 1; Jacobs Wr. D6A[4]). Jacobs is president of Norris (Jacobs 120). Williams is vice president and secretary-treasurer of Norris (Jacobs 122; Williams 162). Williams is president of P-N (Williams 162) and secretary-treasurer of Federated (Williams 162).

3. Respondents Jacobs, Williams and Kenneth Mann ("Mann") are the shareholders and officers and directors of Pan-Am (Compl. Par. 1; Ans. Par. 1). Williams is treasurer of Pan-Am (Williams 163). Mann is vice president of Pan-Am (Mann 213). In addition, Mann is Service Director of Future Motors, a new car franchise dealer in Long Island City, New York, selling Dodge taxicabs and other make Dodge vehicles (Mann 212).

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[2] The content of Mr. Jacob's written testimony on behalf of respondents is not the subject of significant dispute. It should be noted that respondents' counsel deferred his cross-examination of Mr. Jacobs after his testimony on behalf of complaint counsel (160).

[3] It is not clear whether "Garydean" is "Gary Dean" (See Jacobs Wr. D4A).

[4] "Wr" refers to Jacobs' written testimony. "D6A" refers to his answer to question 6 on direct examination by respondents' counsel.

4. Norris is a "gift and novelty" mail-order company selling general merchandise to the consumer (CX 405–7, 409–10). It has been engaged in this business since 1953 (Jacobs 120–1).

5. Pan-Am was in the business of selling cars to consumers by mail (Jacobs 126). It became inactive in 1975 (Jacobs 128; Mann 213). [5]

6. Federated Wholesalers Service - Garydean trading as Nationwide Wholesalers Service was incorporated as one name (Jacobs 128). It was in the business of operating consumer buying clubs, *i.e.* finding persons who were interested in buying merchandise at lower prices, and introducing consumers to mail-order companies located throughout the country (Jacobs 129; see CX 741). Nationwide ceased to operate in 1973; Federated ceased to be active in 1974; and Garydean ceased to operate in 1972 (Jacobs 128–9; Wr. D4A). On several occasions respondents used the name "Nationwide" in "price testing" advertisements in connection with the Norris business (Wr. D12A; D31A; Williams 172).

7. P-N, inactive for the last ten years, was set up to publish a sales opportunity magazine. For a short time it also engaged in the mail-order sale of higher priced general merchandise (Jacobs 127; Wr. D16A). On several occasions respondents have used the name "P.N. Publications" in connection with advertising under their master contract with TV Guide Magazine (see Jacobs Wr. D21A; D24A; see Finding 38).

8. Respondents Jacobs and Williams formulate, direct and control the policies of the respondent corporations Norris, Federated and P-N (Compl. Par. 1; Ans. Par. 1).

9. Respondents Jacobs, Williams and Mann formulate, direct and control the policies of the respondent corporation Pan-Am (Compl. Par. 1; Ans. Par. 1).

10. Respondents Jacobs and Williams, along with others not respondents herein, also have business interests in other mail-order corporations not named as respondents in this proceeding, such as Cheeselovers International, Inc. (Jacobs Wr. D34-44A; see CX 2065) and Overseas Discount Shopping Services, Ltd. (Jacobs Wr. D51-53A).

About commerce and competition.

11. In the course and conduct of its business, Norris causes to be published and mails its catalog to prospective consumers located throughout the United States. In addition, it does substantial national advertising in such magazines as TV Guide and places advertisements in newspapers with interstate circulation (CX 1963;

Jacobs 123). Also, in the course and conduct of its business, Norris mails or otherwise causes the distribution of merchandise to purchasers located throughout the United States. [6]

12. In the course and conduct of its business, Pan-Am causes to be published in the Norris catalog advertisements for its cars. Also in the course and conduct of its business, Pan-Am delivers cars to purchasers thereof located outside the State of New York (see Finding 49).

13. Respondents Norris, Pan-Am and Jacobs, Williams and Mann are engaged "in commerce" as "commerce" is defined in the Federal Trade Commission Act, and business practices relating to the matters alleged in the complaint are "in commerce" and "affect commerce" within the meaning of such terms as set forth in the Federal Trade Commission Act.

14. Respondents Norris, Pan-Am and Jacobs, Williams and Mann are in substantial competition in commerce with others engaged in mail-order businesses distributing and selling various products in commerce (see Jacobs 124).

[NOTE: The term "respondents," as it may appear hereinafter in Findings Nos. 15–48, refers to the Jay Norris Corporation, Joel Jacobs and Mortimer Williams, only (see Discussion, p. 58).]

About guarantees, deliveries, and refunds —

Advertising

15. In the Norris catalogs (see CXs 405, 406, 407, 409, 410) certain statements are made concerning guarantees, deliveries and refunds. For example, the phrase "30 DAY MONEY-BACK GUARANTEE ON ALL PURCHASES" appears prominently on the front cover (CX 409). It is also stated: "Personal Checks: to insure immediate shipment of your order, please have your check certified. Otherwise allow about 2 weeks until your check clears the bank." (CX 409, order blank). On page 33 of CX 409 the following phrase appears: "30 day money back guarantee on all items in this catalog."

Other statements include:

> Your guarantee of satisfaction . . . Everything you buy from Jay Norris Corp. is always first quality. Every item is exactly as described and illustrated. Any item not up to your expectations return in 30 days for full refund (CXs 57, 409). [7]

> Unless item is marked express collect, use this easy chart to figure postage insurance, shipping and handling charges. It's only part of the delivery cost – we pay the rest.

> If your order is up to:

$15.00	add $1.70
$15.01 to $20.00	add $2.20
$20.01 to $30.00	add $3.20
$30.01 to $40.00	add $4.20
$40.01 to $50.00	add $5.20
$50.01 to $60.00	add $6.00
over $60.00	add $7.20

(CX407, p. 52).

16. In the Norris newspaper and magazine advertisements similar statements are made concerning guarantees, deliveries and refunds.

Order now. Christmas Delivery Guaranteed. Mail no risk coupon now. . . . only $9.99 plus $1.00 each for shipping and handling, under your money back guarantee . . . 30-day money back guarantee (CX 2, Flame Gun, Parade Magazine, November 28, 1971). (See also CX 3261.)

30-day money-back guarantee! Mail no-risk coupon now! . . . only 7.99 plus $1.00 each for shipping and handling, under your money-back guarantee . . . prompt delivery guaranteed (CX 4, Flame Gun, Parade Magazine, November 5, 1972.)

Mail no-risk coupon today for a lifetime supply of socks . . . immediate delivery guaranteed (CX 8, Parade Magazine, January 4, 1970.)

Buy with confidence – 30-day Money-Back Guarantee (CX 17, N.Y. Times, October 24, 1971). (See also CXs 20, 24, 25, 44, 67.)

Buy with confidence – Money-Back Guaranteed (CX 28 California Living Magazine, January 7, 1973.)

Use this Jumbo TV Antenna for 30 days at our risk if not completely satisfied return for prompt refund . . . only $1.99 plus 60¢ shipping and handling under your money back guarantee (CX 886, 1–46 Jay Norris, 1975.)

[8] Order by mail with confidence – 30 day money back guarantee (CX 62, Parade Magazine, August 12, 1973 Lincoln-Kennedy Penny.)

Use these products 30 days at our risk. If not completely satisfied, return for refund. (CX 96A–D, Parade Magazine, February 9, 1975.)

90 Day Money Back Guarantee . . . you may return within 30 [90] days for prompt refund of purchase price (CX 117 A, H, Parade Magazine, March 14, 1976.)

Try this bait oil 30 days at our risk, if not completely satisfied, return for prompt refund (CX 386, New York City Metro T.V. Guide, February 15–21, 1975).

Representations

17. It is found that, through the printed statements contained in respondents' catalogs, newspaper and magazine advertisements, as well as various communications to persons who have ordered

merchandise, respondents have, as alleged in the complaint, represented directly or indirectly, that:

a. merchandise paid for by a certified check is shipped to purchasers immediately;

b. merchandise paid for by a non-certified check is shipped to purchasers about two weeks after said check has been approved for payment at the purchaser's bank;

c. the full purchase price of the product plus all additional charges paid by the purchaser in connection with said purchase are refunded by respondents if the purchaser is dissatisfied for any reason;

d. a sum of money in the form of cash, check, money order or other negotiable currency is refunded to purchasers if they are dissatisfied for any reason; [9]

e. pursuant to respondents' 30-day money back guarantee, purchasers will receive a full refund if the merchandise is returned to respondents within 30 days from the date of the purchaser's receipt of said merchandise;

f. in a substantial number of cases, the non-delivery of the purchaser's order, is caused by the loss of the merchandise by the United States Postal Service;

g. purchasers of respondents' products pay only part of the delivery cost and the respondents absorb the remaining portion of said cost;

h. exchanges or refunds are expeditiously processed by respondents; and

i. all parcels shipped to purchasers, except those items marked express collect, are insured against loss, damage or other casualty by respondents.

Consumer testimony

18. Complaint counsel presented consumer witnesses who testified about their prepaid mail-orders from respondent Norris and problems concerning delayed delivery or non-delivery of the merchandise ordered.

On January 8, 1973, Andrew Littlejohn ordered a flame gun from Norris by mail, paying for the merchandise by postal money order. A month later, having not received the ordered merchandise, Mr. Littlejohn wrote to Norris, but received no reply. Receiving no reply to subsequent letters, he contacted the Post Office Department and the Better Business Bureau. On May 3, 1973, he received the flame gun (337–339; see CX 3233).

Frank Trupia ordered a TV Antenna by mail from Norris on April

10, 1973 (332; CX 4251E). Not having received the merchandise by June 1, Mr. Trupia wrote to Norris. Receiving no response, Mr. Trupia, at the end of June, wrote to Norris again, threatening to take the matter to the Better Business Bureau. Norris responded to the second letter and in August Mr. Trupia received the ordered merchandise (332–334). [10]

In early 1973 Lester Colodny ordered a two drawer file from Norris, by mail (see CX 3091). After he wrote several letters, he received a form notice two months later and sometime after that received the merchandise (347–349).

Lois Johnson ordered a tool set from Norris by mail. She paid by certified check (3188). When she did not receive the merchandise after 4–6 weeks, she wrote to them. Norris sent her a post card response (CX 3190A, B dated August 27, 1975). When she still did not receive the merchandise she wrote again and received another post card response requesting information about the order (CX 3190C, D dated January 2, 1976). Miss Johnson did not answer the second card and never received the ordered merchandise (411–419).

Jeffrey Feldman ordered a socket wrench and tool set from Norris by mail on March 16, 1973 (CXs 3129AB, 3130). When he received his bank statement he noticed that his check had been cashed by Norris. Not having received the ordered merchandise, he wrote to Norris, but received no response. He wrote several more letters to Norris and received no reply. He then wrote to the Federal Trade Commission and, thereafter, received the ordered merchandise in the first week of June 1973 (424–429).

On March 24, 1974, Richard Waysse ordered a tube of glue from Norris by mail (CX 3320AB). On April 24, 1974, not having received the ordered merchandise, he wrote to Norris requesting the merchandise or a refund. He received a post card from Norris advising him to wait four weeks after the original order (CX 3321C). On May 24, 1974, Mr. Waysse requested Norris to send him a refund (CX 3323). He refused to accept the package from Norris when it was delivered in the latter part of June 1974 (435–439; see CX 3330). He subsequently received a refund on July 22, 1974 (CX 3334).

On November 5, 1973, Mr. White ordered a wrench and tool set from Norris by mail. After he inquired about delivery, Norris advised him that they were out of stock (453–456; see CXs 3358, 3359AB). He never received the merchandise (456, 459). [11]

On December 4, 1973, Mr. Henick ordered two sets of "Everything Organizers" from Norris by mail (483; CX 3173). He never received the merchandise although Norris was advised of the failure of delivery (see 487, 493; CXs 3173, 3178).

Clara Zappa ordered a "five-year" flashlight from Norris by mail in January 29, 1973, and when she did not receive the merchandise by May 1, 1973, she contacted the Better Business Bureau. She received the flashlight in May 1973 (529, 531-3; CX 3365, 3366).

Angela Martone ordered "Spanish Fly" fishing lure bait from American Value in February 1975, and after writing four letters to American Value[5] requesting shipment or a refund, she contacted the Better Business Bureau and in September 1975 received the merchandise (543-47, 549; CX 3256AB).

Allen Carreau ordered a solar blanket in April 1973. Norris requested he remit an additional 50¢, which he did (CX 3074). He did not receive the merchandise until December 1973 or January 1974 after he had contacted Norris in June, and, receiving no reply, the Better Business Bureau in October (551-556; CX 3073).

Charles Silverman ordered a tool set from Norris by mail early in November 1973. In January 1974 he wrote to Norris twice advising that he had not received the merchandise, and receiving no response to either letter, contacted the Better Business Bureau on January 8, 1974. He then received a communication from Norris and received the merchandise in May 1974.

Leslie Gordon ordered a book from Norris by mail in February 1973 (CX 3168). When he did not receive the merchandise he wrote to Norris in March, but received no reply (570-1). After he wrote to the Attorney General of New York, he received a post card from Norris in April or May advising that they were going to ship the book, but he never received either the merchandise or a refund (572, 574).

In November 1971, responding to an advertisement that guaranteed delivery by Christmas, Frank Matullo ordered a [12] flame gun by mail from Norris (CX 3060B, 3261). When he did not receive it, he wrote to Norris, but received no response. After he complained to the Better Business Bureau in March 1972, he received a card from Norris, and a few weeks later received the flame gun (576-586).

On March 29, 1974, Catherine Cunningham ordered a socket wrench tool set from American Value by mail (CX 3095-6). In two weeks she received a card from Norris advising that there would be a delay in shipment. When six months passed and she still had not received the ordered merchandise, Mrs. Cunningham, in November, wrote to Norris, but received no response. Again in January she wrote to Norris but received no answer. After contacting the Better Business Bureau, she received a letter from Norris (CX 3098). She supplied the information requested and in three or four weeks (in February or March of 1975) received the tool set (617-621).

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[5] For findings on "American Value," a trade name used by Norris when advertising in TV Guide, see Finding 37, *infra.*

Andrea Discepolo, in May of 1974, ordered a "moon mission" blanket from American Value by mail. Not receiving the ordered merchandise after ten months she wrote to American Value, but received no response. She wrote again a month later, but received no response. Four to six weeks after contacting the Better Business Bureau she received the product (629-637; CXs 3114, 3115).

In March 1973, Arthur Fink ordered some "miracle cement" from Norris, by mail. He wrote to Norris in May advising that he had not received the ordered merchandise, but received no response. He wrote again and received a letter from Norris asking for details about his order. Not receiving the merchandise by June, he wrote again requesting a refund. In July he contacted the New York Times, the newspaper in which the Norris advertisement appeared, and thereafter he received the merchandise (657-660).

At the end of January 1973, Henry Flury ordered two sets of tools from Norris by mail, responding to an advertisement in the New York Times (668). He received the merchandise in the beginning of April after he had cancelled his order and requested a refund (670).

On January 15, 1975, Jeffrey Simkowitz ordered "a couple of stainless steel [measuring] tapes" from Norris by mail (see CX 3305A). Three months later, not having received the ordered merchandise, he wrote to Norris. They responded by card telling him to wait four weeks from the time he sent in the order (CX 3305B). On May 30, 1975, [13] he contacted the Better Business Bureau and in June received a communication from Norris stating that if he wanted a refund he should send them the cancelled check but if he received the tapes in the meanwhile to disregard their letter. He received the tapes in the middle of June (677-683).

In 1975, John Clampet ordered an "Aztex Pendant" from American Value by mail (685-6; see CX 3080). When he did not receive the ordered merchandise and could not contact "American Consumer" by telephone, he contacted the Better Business Bureau. Thereafter Norris contacted him and advised that the product had been reshipped. Mr. Clampet never received it (688-689; CX 3084).

On April 24, 1974, John Amato ordered a pair of "Swedish scissors" from Norris by mail. After not receiving the ordered merchandise for three weeks, Mr. Amato wrote Norris and received a reply that there was a delay due to a strike. He sent two other letters and received other "excuses" (693-694, 697; CX 3041, 3042). In June, he finally received a pair of scissors (695).

On January 28, 1973, William Veale ordered a set of tools from

Norris by mail (703; CX 3318). Not receiving the ordered merchandise in four or five weeks, Mr. Veale wrote to Norris, but received no reply. He again wrote to Norris two or three weeks later, but received no answer (705). He thereafter secured a refund after contacting the Consumer Affairs Office, State of New York (705-6; see CX 3319).

In February 1975, Gloria Gebel ordered a Monaco shaver from Norris, by mail (776-7). In March, having not received the razor-shaver, she tried to contact Norris by telephone and when that proved unsuccessful she complained to the Better Business Bureau (779). The merchandise was delivered at the end of March or early April (779).

On October 1, 1975, Peter Sanchez sent his check for $21.49 to Norris, ordering a shaver-razor by mail (789-90; see CX 3288). When Mr. Sanchez had not received the ordered merchandise by October 30, 1975, he wrote to Norris on that date demanding a refund (791). He received the shaver two or three days later (792). [14]

On June 10, 1975, Bethuel Webster sent his check for $14.99, and on June 24 a check for an additional 70¢, to Norris, ordering a pair of sunglasses by mail (CX 3337). On July 30, Mr. Webster wrote to Norris advising that he had not received the ordered merchandise (1192). On August 19, 1975, having not received a response to his July 30th letter, he sent to Norris a copy of that letter. Norris responded by post card, received by Mr. Webster August 20, advising that the sunglasses should be received shortly. Having not received the ordered merchandise by September 3, 1975, Mr. Webster requested a refund or the ordered product (CX 3342). On September 10, 1975, Norris requested verification of the purchase (CX 3339). Mr. Webster responded and received the merchandise about October 10, 1975.

In November 1974, Francisco DeLima ordered from Norris by mail a refrigerator defroster and some pairs of socks (1205). Having not received the ordered merchandise Mr. DeLima contacted the Consumer Affairs Office (New York City) in January 1975 and the Consumer Affairs Office (Nassau County) six months after placing his order. Norris then communicated with him asking whether to still ship the merchandise. He responded "no" and advised them that he wanted his money back.

19. Respondents also presented a number of consumer witnesses. They testified that in response to advertisements in newspapers, and in two instances, catalogs (see Nierenberg 1792; Trial 1794), they had ordered various items of merchandise by mail from Norris and had received the ordered merchandise anywhere from a week to four

weeks, but in most instances from 10 days to two weeks (Horn 1623–5: in 1974 or 1975, "wall plaque," "plastic container for milk carton," "artificial flowers;" Burns 1632–33: in 1974 or 1975, "graffiti remover," "rust buster;" Curley 1641–2: in 1975, "hose connection;" Nelson 1647–8: in 1976, "magic window cloth;" Calderaro 1649-50: in 1969, 1972 and 1973, "weather zone," "opera glasses," "clip-on glasses;" Dulsky 1658–9: in 1972, 1974 and 1976; "framed pictures," graffiti remover," "rust buster;" Ferrari 1668: in 1973, "heating pad;" Shands 1674–76: in 1973 or 1974, "book;" Vercy 1680–2: in 1974, "hose nozzle;" Brown 1685: in 1976, "graffiti remover;" Kefer 1785–87: from 1972 to 1976, "hose nozzle," "adhesive," "wall duster;" Nierenberg 1791–3; in 1974 or 1975, "happy home recipe;" Trial 1793–4: in 1974, "wall hanging;" Lengyel 1796–7: in 1975, "carving knives;" Lowery 1797–8: in 1974, "graffiti remover;" Edwardson 1813–4: in 1975, "Make-A-Log;" Sabatino 1814–5 in 1975, "sissors;" Dyer 1816–8: in 1974 and 1976, "vegetable slicer," "car brushes"). These consumer witnesses were [15] satisfied with the delivery of their orders. To the same effect see affidavits of 21 other consumer witnesses (RX 11–31).

Consumer Agency evidence

20. Several "Consumer Agency" witnesses testified as to the nature of complaints lodged against Norris. Mr. Vincent, account executive for TV Guide, testified that over the two-month period that TV Guide analyzed customer inquiries on Norris advertising, they received 50 complaints almost all (98%) of which related to "late delivery" (837).

Evelyn Vargas, an employee of Parade Publication, a Sunday supplement distributed in newspapers throughout the United States, testified that she handled letters of complaint received by Parade (905). Her tabulation of complaints relating to Norris, compiled at the request of the Federal Trade Commission, indicated that most of the complaints related to failure to deliver merchandise (CX 2484; see also CX 2485).

Ruth Ann Marsden, an investigator with the Nassau County Office of Consumer Affairs (927) testified she handled all Norris complaints and in 1975 wrote a report concerning such complaints (938–9; CX 2495). Many of those complaints related to nondelivery or late delivery and failure of Norris to respond to letters sent to them by customers inquiring about their orders (949, 966, 988; CX 2495 C–E).

Jean Bozek, an employee of the Long Island Better Business Bureau, who handles letters of complaint in the course of her duties, testified that she tabulated complaints relating to Norris concerning nonreceipt of merchandise and nonreceipt of refunds (999, 1014).

About respondents' handling of mail orders

21. The day the mail is received it is opened. If the order is in response to a "space advertisement," that is an advertisement placed in a magazine or newspaper instead of the Norris catalog, it is sorted by department number. The orders are also separated according to products and are sent to "key punch" that same evening (Jacobs 135-6). On the second day the order is "key punched," *i.e.,* certain information is encoded onto a computer card (136). On the third day the order goes to the computer service, Harbor Computer Systems, located in Hicksville, New York. On the [16] third or fourth day the computer service returns a shipping label to Norris. Most orders on "space advertisements" are shipped on the fourth day (Williams 181). A computer memory record is kept of the customer's name, address and the product purchased (136).

In the case of catalog orders, only the customers' name and address, the date received and the amount of money remitted are put in the computer memory (182). Catalog orders, which are handled manually, are given to the personnel in the warehouse as soon as the order is opened and the information to be sent to the computer service has been recorded on the envelope (183).

A record is made in the "cash book" of all orders as to the date received and the amount of money sent in by the customer(184-186). Although separate records are kept in the cash book for "space" sales and "catalog" sales, all monies received are deposited to the same bank account (184).

Otherwise, Norris does not keep actual records of the customers' orders (186). In most instances (perhaps 80%) shipments to the customers are made through the United States Postal Service, the rest being shipped by United Parcel Service, when it is more economical to do so (Williams 185).

Respondents are self-insured; that is, instead of paying for public insurance on shipments, they make shipments at their own risk. Because they cannot trace shipments, they make all necessary replacements at their own expense and at no charge to the customer (Jacobs 146-7; Williams 200).

About respondents' handling of customer inquiries about nondelivery

22. Respondent Jacobs testified as follows regarding Norris'

response to customer inquiries relating to nondelivery of merchandise (140-1):

> . . . The mail arrives. The girl opens it. She looks at it and she reads the customer's complaint. Assuming that there is a date on which the customer says she ordered, the girl checks the records and determines whether or not that order should have been shipped.
>
> If sufficient time has elapsed for the . . . order to have been shipped, assuming that the customer hasn't complained too quickly before she would have had a chance to receive it, the girl will send a delay notice saying that if we received your order, it should have [17] arrived by the time you receive this notice or it will be arriving soon. Please allow another few days. If you still don't have it, let us know, so we can trace it.

Mr. Jacobs added that if respondents become aware of a delay in delivery of merchandise by a manufacturer to Norris, they "notify the customer that there is going to be a delay and tell her we expect to ship within a matter of time" (142).

In this respect, in the course and conduct of their business, respondents use form notices printed on post cards by which they make various responses to customers inquiries about delivery (see Williams 195, *et seq.*) One such card reads as follows (CX 4246; see also CXs 3305B, 3321C, 3338A-D):

> Dear Customer:
>
> Your order should have arrived by this time. However, actual delivery time varies tremendously and, unfortunately, is entirely out of our control once the shipment leaves our warehouse. It is possible that it is still enroute to you.
>
> Please bear in mind that it often takes the best part of a week after mailing before an order reaches us. Then it takes a few days to process it. Since shipments are made via Parcel Post or where possible, United Parcel Service, delivery might take as long as another two weeks.
>
> We suggest you allow a total of at least four weeks from the time you mail us your order until you receive it. By now, we feel confident your shipment is either in your hands, or will be within the next few days.
>
> We are sorry for the inconvenience and appreciate your patience and understanding.
>
> Sincerely,
>
> /s/
> Rhea Nichols
> Customer Service

[18] Another form post card used by Norris in response to a complaint of nondelivery of merchandise reads as follows (CX 4245):

> Dear Customer:
>
> We received your letter that you did not receive your order. You did not give us all

the information we needed to check your order. Please supply us with the following information.

Date you mailed order ________________
Merchandise ordered ________________
Amount of your check ________________
or money order ________________

This matter will be given our immediate attention.

Thank you

/s/
Rita Andrews
Customer Relations

Another form post card used by Norris where shipment might have been delayed is CX 4243:

Re:

Dear Customer:

We are sorry there was a delay in shipping your order. It was caused by circumstances beyond our control. If you have not yet received the merchandise, please wait another week. If by that time you still have not gotten it, please indicate so below and return this card to us. We will then place a tracer with the Postal Authorities and a duplicate shipment will be made.
Thank you

/s/
Claris Walters
Customer Relations

[19] Another form post card used by Norris where nondelivery is involved is CX 4248:

This Card is Worth $1.00 to you! See Below!

Dear Customer:

We are sorry that you did not receive the merchandise you ordered. It obviously was lost in transit.
We are sending a duplicate shipment at once. You should be receiving it within the next 2 or 3 weeks or sooner.
Thank you.

/s/
Evelyn Barnes
Customer Relations

P.S. If you return this card with your next order you may deduct $1.00.

Nondelivery was sometimes due to the ordered item not being in stock. An example of a post card used in such circumstances reads as follows (CX 3041a):

Dear Customer:

Thank you for your recent order.

Due to unusually heavy demand, the item you ordered is temporarily out of stock. More is expected soon. Just as soon as the new shipment arrives, your order will be rushed to you.

I'm sure that when it arrives, you'll be delighted with it and you will find it was well worth waiting for.

Thank you.

/s/
Rhea Nichols
Customer Service Dept.

[20] Another form post card used by Norris in 1973 reads as follows (CX 3092):

Dear Customer:

Thank you for your recent order.

Due to unusual circumstances beyond our control, there will be a short delay in shipping your recent order of our product. We appreciate your patronage and consider you a valued customer.

We will do everything possible to expedite your current order.

Please do not write. We will ship your order in two weeks or write to you again.

Respondents do not check the customers order against the information stored in the computer which they use. (see Williams 201).

About the number of customer complaints

23. Norris' annual volume of sales is approximately $13,000,000 (Jacobs 123). This involves the processing of approximately 2,000,000 orders a year. In 1976, the number of complaints received from customers was about 2% of the total orders (Jacobs 148).

In 1975, the number of complaints was approximately 2-1/2% of a total of 2,000,000 orders and in 1974 the number of complaints was approximately 3% of a total of 1,500,000 orders (Jacobs 149). Generally, Norris does not retain copies of customers' letters of complaint (Williams 189).

Unfair and deceptive practices

24. During the period of time relevant to this matter, respondents on numerous occasions have deposited customers' checks or cashed money orders, and have not shipped the ordered merchandise for many months after their receipt of the order and payment.

(Johnson 411, 418; Feldman 427; Waysse 437, 439, 442-3, 446; White 455-6; Henick 485-87, 491-2; Littlejohn 337-9; Colodny 349-50; Zappa 532; Martone 543, 545-6; Carreau 554-5; Silverman 566-7; Gordon 571; Matullo 577-9; Cunningham 620; Discepolo 633-5; Turk 658-60; Simkowitz 678-9, 682; Gebel 777-9; Sanchez 789-92; Clampet 687-9; Amato 693-5; Veale 704-5; Webster 1187, 1190-4, 1196; Delima 1205-6, 1211). [21] Respondents' representations that they ship merchandise "immediately" or in about "two weeks" are false and misleading. Moreover, receipt and retention of monies for merchandise not promptly shipped, is an unfair act or practice (see Feldman 427; Waysse 440; White 453; Henick 486; Littlejohn 338; Zappa 531; Martone 545; Silverman 567; Gordon 571; Matullo 577).

About refunds

Consumer testimony

25. Complaint counsel presented several witnesses who had requested refunds from Norris either because they were dissatisfied with the merchandise and had returned it or because they had not received the merchandise ordered.

Lester Colodny returned, by mail, the files he had ordered from Norris, requesting his money back (351; see CX 3091). Not hearing from Norris after writing "letter after letter" he wrote to the New York Times (CX 3090). Nine months after requesting the refund, Mr. Colodny received it (354). The amount of the refund was the amount he sent to Norris with his order (359).

Ralph Marino ordered and paid $19.99 plus tax, sales tax, postage and handling for a shaver from Norris in June 1975 (362, 364). Being dissatisfied, he returned it by mail to Norris (366). He received a partial refund of $19.99 in about four weeks (367, 385; CX 3249). Later he received an additional $3.10, the amount of taxes and handling charges (390-2; CX 3248A).

In July 1974 Alfred Langella ordered from Norris, and paid $7.21 for an orthopedic driver's seat for an automobile. Not being satisfied, he returned it promptly, requesting a refund (397-98). Failing to hear from Norris, he telephoned them (398-9). Getting no satisfaction from that contact, Mr. Langella contacted the Long Island Better Business Bureau, the New York Times and the Federal Trade Commission requesting help in securing his $7.21 plus shipping charges for the return of the merchandise (399; see CX 3206). Thereafter, in late October, he received a refund from Norris in the amount of $7.21 which was the amount that he had requested from Norris (401). [22]

When Jeffrey Feldman did not receive the tool set that he had ordered from Norris and paid $14.98, he wrote to Norris in May requesting delivery or a refund. Not receiving any reply from Norris he contacted the Federal Trade Commission (428). In the first week of June he received the tool set (429). Being dissatisfied with the product, Mr. Jeffrey returned it to Norris, requesting a refund (433). He again wrote to Norris in July requesting his money back (430). He finally received the amount that he had sent to Norris at the end of July or early in August (430, 434).

Richard Waysse testified that he refused to accept packages from Norris after he had demanded a refund of $2.57. Eventually, he received a refund after writing to many consumer agencies (444; see CX 3334).

John White testified that after he was notified by Norris that they did not have the tool set he had ordered in stock, he requested a refund. He never received either the merchandise or the refund (456, 458).

Bernard Henick testified that he requested a refund because the merchandise he ordered was never delivered to him, but he never received the refund (493).

Bruce Peters returned certain merchandise to Norris he had ordered in January 1974 (516; CX 3267). Not receiving the refund after three weeks, he wrote to several consumer agencies (518). In August 1976, at the suggestion of the attorney who was complaint counsel in this matter at that time, Mr. Peters wrote to respondent Joel Jacobs and promptly received a refund of the amount he had paid to Norris ($23.58) (519).

Angela Martone testified that she wrote to Norris in March 1975 about nondelivery of merchandise and requested a refund if they did not have the merchandise. She received the merchandise in September 1975, after contacting the Better Business Bureau (545-46,549).

Arthur Fink testified that he received the ordered merchandise after he had requested that Norris make a refund (659-62). [23]

Henry Flury testified that he received the merchandise he ordered from Norris after he had requested a refund, having not received the merchandise within a reasonable time (669-70). He returned the merchandise to Norris and received a partial refund ($25.00) after contacting the New York Times and the Better Business Bureau (670). Later he received the balance of the refund ($5.98) (673).

Jeffrey Simkowitz testified that he received the merchandise ordered after he had requested a refund from Norris because of nondelivery (683).

John Amato testified that he returned certain merchandise to Norris for a refund of $4.93 (693). About two months later Norris advised they would make a refund, and sent a money order for $2.00 and stamps, which amounted to 13¢ less than the total amount he had paid to Norris (696).

William Veale testified that upon nondelivery of merchandise he secured a refund of $12.00, $2.00 less than the amount he paid Norris, after contacting the Consumer Affairs Office (705-6).

Gloria Gebel returned a shaver-razor to Norris at the end of March or early April. After contacting the Nassau Consumer Affairs Office towards the end of April, in about two weeks she received the refund ($19.95) which was less than the amount she had paid Norris ($22.89) (782). She did not pursue the matter further (784).

Peter Sanchez testified that he received the ordered merchandise from Norris after he had requested a refund because of nondelivery (791-2). Being dissatisfied with the product, he returned it in early November to Norris and demanded a refund (793-4). After complaining to the Postal Authorities he received a refund check dated November 24, 1975 ($21.49) (795).

Francisco DeLima received a refund from Norris upon request after the merchandise he ordered was not delivered and after he had contacted the Nassau Consumer Affairs Office (1208).

John Dierenger returned a product to Norris with which he was dissatisfied and received what he considered to be a partial refund. After writing to the Better Business Bureau, Norris refunded the balance of 47¢ plus 1¢, in the form of postage stamps (1229), which represented the amount of postage he had paid to return the product to Norris (1233; see CX 3111). [24]

Richard Scully returned a damaged kite that he had ordered in April 1973 from Norris three or four days after receipt (506-7). He received a second kite in November after contacting the Better Business Bureau, Long Island (508; CXs 3299, 3300, 3301).

About respondents' handling of customers' requests for refunds

26. Respondent Jacobs testified that, generally, returns are opened within a matter of two or three days after the parcel arrives (at most seven days during "peak season"). The parcel is opened and duly recorded at which time the girl is actually writing the customer's refund check and an apology.

If a complaint comes in on a refund, the girl would write the customer and state that if Norris received the returned package the refund was made promptly and the customer should be receiving it soon (141-2; Wr. C2A).

The form post card used for the purpose of responding to complaints on refunds is CX 4247:

> Dear Customer:
>
> We are most anxious to clear up the inquiry about the merchandise you returned to us. If we received it, a refund or exchange was made as you requested. If you did not receive a refund or exchange, we must assume that we never got your package. We suggest you contact the postal authorities and place a tracer on this shipment.
>
> Thank you.
>
> /s/
> Re: Mrs. B. Marks

Jacobs testified that it is respondents' policy to refund the sales tax along with the price paid for the merchandise and any instance where this was not done might be attributed to human error (Wr. D1A, D2A). He further testified that stamps have been sent as a refund "on rare occasions when the amount being sent is under $1." Credit certificates are issued only on catalog orders for multiple products when respondents are out of stock on a particular item. The customer is given the option of returning the certificate for cash or using it toward future purchases (Wr. C1A). [25]

Jacobs testified that Norris processed about 800 requests for refunds every week in 1976, and that before that, during the 1970s, the total may have been around 1000 requests for refunds per week (Wr. C3A).

Jacobs testified that respondents' policy is to handle these refund requests promptly, in a matter of days (Wr. C4A, C5A).

Respondents do not check the customers order with the information stored in the computer that they use (see Williams 202).

Unfair and deceptive practices

27. Respondents do not always refund the full purchase price of the product plus all additional charges paid by the purchaser in connection with said purchase (Marino 367, 385; Veale 705–6). In many instances respondents deduct the "handling and delivery" charge (Marino 377–8; Flury 670–5; Gebel 782–4; Veale 706; Dieringer 1229–30). Accordingly, respondents' representation that the full purchase price of the product plus all additional charges paid by the customer in connection with said purchase are refunded by respondents, if the purchaser is dissatisfied for any reason, is false and misleading.

28. Respondents do not always refund the sum of money in cash, check, money order or other negotiable currency, but issue credit

certificates or enclose stamps in connection with certain refunds (Amato 696–701; see Jacobs Wr. C1A; Resp. PF pp. 12–13). Accordingly, respondents' representation that they make refunds in cash or check or other negotiable currency is false and misleading.

29. Respondents do not always make a full refund, and sometimes have failed to make any refund, to purchasers who have returned the products within 30 days of their receipt thereof (Colodny 351–4; Marino 367, 385; Langella 397–401; Feldman 428–34; White 456–8; Henick 493; Peters 516–9; Sanchez 791–5). Accordingly, respondents' representation that they give a "30-day money back guarantee" is false and misleading. [26]

30. In several communications with customers respondents have requested that nondelivery of the customers' orders is due to the loss of the merchandise by the United States Postal Service (see CX 4248; Finding 22, *supra*). However, respondents, before making such a representation, do not ascertain whether such product has been shipped, but merely assume that it has (see Findings 21, 22, *supra*). In many instances the ordered merchandise has not been shipped. Accordingly, respondents' representation that nondelivery is due to the fault of the United States Postal Service is false and misleading.

31. There is no evidence of record to show what share of the cost of delivery is paid by respondents or their customers. Thus it cannot be determined whether respondents' representation that they absorb a portion of the delivery charges is true or false.

32. In some instances refunds are not expeditiously processed by respondents. Many purchasers have encountered long delays, sometimes constituting many months before receiving their refunds. Many purchasers' refunds have been secured only after they sought assistance from consumer protection agencies or local, state, and federal government agencies (Waysse 444; Peters 516–9; White 456, 458; Henick 492; Colodny 351, 354; Marino 377–8; Scully 507; Fink 659; Flury 669–70; Langella 398–400; Sanchez 791; Amato 696; Veale 706; DeLima 1207; Dieringer 1229).

33. Respondents are self-insured. Their representation that the purchasers merchandise will be shipped insured is false and misleading.

About respondents not answering customers' inquiries and complaints

34. Respondents, on numerous occasions, have failed to answer customers who have written to them complaining of nondelivery of merchandise ordered and paid for (Trupia 333; Littlejohn 337; Jeffrey 427–8; White 463; Henick 487, 492; Martone 545–6; Carreau

554; Silverman 566; Matullo 579; Discepolo 634; Clampet 687-8; Veale 705; DeLima 1206). In other instances respondents' replies have not responded to the customers' complaint, but have tended to delay and prevent customers from seeking delivery of merchandise or refund of money (Johnson 412-6; Waysse 437-43; White 455-6; Henick 487, 492; Colodny 351; Martone 545-6; Carreau 554; Silverman 566; Gordon 571-2; Matullo 579; Cunningham 620; Discepolo 634-6; Fink 659; Flury 671; Simkowitz 679, 683; Langella 398-9; Sanchez 795; Clampet 689; Amato 694; Veale 705; Webster 1193-5; DeLima 1206-7, 1211). [27]

About respondents not listing their telephone number

35. Respondents do not have the Norris telephone number listed in the Nassau County telephone directory, and many customers who have attempted to contact Norris by telephone have been unable to do so (Trupia 332; Feldman 427; White 456, 459; Scully 506; Peters 515, 525-6; Zappa 531; Carreau 559, 563; Silverman 568; Matullo 579; Discepolo 634; Clampet 687-8; Amato 695, 699; Gebel 778, 785; Sanchez 790; Dierenger 1228). Some customers were able to reach Norris by telephone (Langella 400; Henick 501; Gebel 782).

About respondents requiring customers to make proof of purchase

36. In certain instances, in response to complaints by purchasers about nondelivery of merchandise or failure of respondents to make refunds, respondents have required the purchaser to submit details concerning the transaction (see Williams 189). In cases of nondelivery, respondents request the cancelled checks, order blanks and a full description of the merchandise ordered (see CX 4245; Finding 22, *supra*). In cases involving demands for refunds, respondents require the purchaser to submit proof of purchase and proof of the return shipment to Norris, namely the insurance receipt (see Williams 201; see CX 4247).

About respondents' advertising in TV Guide

37. The J. Morton Williams Advertising, Inc., ("Morton") is the "in-house" advertising agency of Norris (Jacobs Wr. D22A). Its officers are Jacobs and Williams (Malfitano 234).

Before 1975, Norris advertised in TV Guide under the name "American Value." Actually Norris placed this advertising through "American Consumer," a competing mail-order business (Jacobs 124; Malfitano 243, 269; CXs 386, 389, 1808D), in order to take advantage of lower advertising rates that "American Consumer" could offer as part of its master advertising contract with TV Guide (Jacobs Wr. D13A, D14A).

In 1975, Norris entered into its own master contract with TV Guide. Morton placed not only Norris advertisements to be published in TV Guide, but also handled insertion orders for other sellers (Malfitano 238, 267). In this [28] respect, it notified TV Guide, as it was required to do, of the various names under which advertising would be placed under the contract (Jacobs 134, 138; Wr. D23A; Williams 167, 170; Malfitano 261). These names included Value House (CX 645, 646, 649); Fashion Scene (CX 667); Unique Ideas (CX 669); Deter Stop Smoking Plan (CX 694, 867); House of Values (CX 699, 868, 2754); and Fashion Scene & Value Corner (CX 706, 868). (See also Jacobs Wr. D24A, D25A). Morton bills these other advertisers (Malfitano 248). The merchandise ordered under these names by purchasers were shipped by the other sellers, not Norris, the address on the coupons not being that of Norris (Malfitano 247; see CXs 2783-90, 2792-3, 2795-2801, 2804-5). Norris never used these names in advertising its own products (Jacobs Wr. D26A, D27A).

On July 30, 1975, Roslyn Malfitano, an employee of Norris who described her duties as Advertising Director (233) wrote the following message to TV Guide from Morton (CX 866):

> This is to advise you that the following companies all divisions of the Jay Norris Corp., are entitled to be covered under the Jay Norris Master contract:
>
> P.N. PUBLISHING, J. MORTON WILLIAMS ADVERTISING INC., FEDERATED WHOLESALERS, VALUE HOUSE, UNIQUE IDEAS, AGGRESSI VESTOR, FASHION SCENE, CHEESELOVER'S INTERNATIONAL.

Subsequently, on February 17, 1976, she wrote the following message to TV Guide (CX 869):

> Please be advised that Jay Norris Corp. has a major interest in the Adventurers & Radio Club.

Apparently Miss Malfitano's description of the relationship between Norris and the named organizations was to qualify them as advertisers, and was not intended to reflect a legal relationship (Malfitano 244, 263; Jacobs D28A, D29A, D32A).

About respondents' other advertising

38. Occasionally, Norris will advertise under another name. "Nationwide Wholesalers Service" was used to test a price (Williams 172). However, "P.N. Publication" was used in connection with another seller's advertising via the Norris-TV Guide contract (Jacobs Wr. D21A). [29]

J. Norris advertisements were run by out-of-state publishers, contracted by an agency to supply such advertising to publications of limited circulation. Sometimes, a local address would be used and the publisher or the agency would send the orders in bulk to Norris for filling (Jacobs 139). This did not constitute over 2% of Norris' business (Williams 176).

About Cheeselovers International

39. Cheeselovers International is a separate corporation. For a short time it had offices in the Norris Building, but has since "moved" to Westbury, Long Island, where it maintains a separate mailing address (Wr. D41A). During the time it was located in the Norris Building, Cheeselovers International had its own employees and paid all of its own bills (Wr. D42A, C14A, C15A, C16A; see CX 2065).

About respondents' mailing addresses

40. Respondents do not use post office box numbers; in fact now they have their own zip code, and the United States Postal Service provides a portable trailer substation for the handling of Norris mail (Williams 174-75).

Some of the mailing addresses used by Norris on the coupons which appeared in the various advertisements for Norris' products follow: American Value, Norris Bldg. 25 W. Merrick Rd., Freeport, N.Y. 11521 [February 1975] (CX 386); Jay Norris Corp., 31 Hanse Ave., Freeport, N.Y. 11520 [November 1971] (CX 2); [November 1972] (CX 4); [January 1970] (CX 8); Jay Norris Corp., 85 Henry St., Freeport, N.Y. [October 1971] (CX 17); Jay Norris Corp., 25 W. Merrick Rd., Freeport, N.Y. 11520 [1972] (CX 24); [1974] (CX 25); American Value, 25 W. Merrick Rd., Freeport, N.Y. 11520 [June 1973] (CX 26); Jay Norris Corp., 25 W. Merrick Rd., Freeport, N.Y. 11521 [1975] (CX 886).

In 1973, Norris' business mailing address was 31 Hanse Ave., Freeport, N.Y. 11520 (see CX 3301) and in 1976 it was 31 Hanse Ave., Freeport, N.Y. 11521 (see CX 3190C).

About respondents' various business styles

41. In the complaint it is alleged that respondents used numerous corporate names and various post office box numbers and addresses in such a manner as to create confusion in the minds of purchasers who are unable to relate all the names used to Norris or to its principal owners (Par. 13(e)). **[30]**

The names listed in the complaint are Jay Norris Corporation, P.N. Publishing Corporation, Norris Nutrition, Garydean Corp., Federated Nationwide Wholesalers Service, Federated Wholesalers Service, Nationwide Service, Cheeselovers International, Pan American Car Distributors Corporation, Associated Auto Wholesalers Corporation.

This charge is not sustained by the record in this case. It does not appear that respondents tried any subterfuge in the use thereof. The only confusion of record arose from the use of "American Value" by Norris during the time when Norris was advertising under the American Consumer master contract with TV Guide. Several consumers testified that they did not know they were dealing with Norris (White 456-9; Martone 544; Cunningham 617, 622-5; Discepolo 629, 635, 639; Clampet 684-91). In my opinion this does not amount to an unfair or deceptive practice within the meaning of the Federal Trade Commission Act. Moreover, there is nothing unlawful about a company offering reduced advertising rates through its master contract. In any event, the complaint does not charge that respondents have hidden the identity of other sellers by use of respondents' various trade names.

About respondents' representations as to the performance, efficacy or characteristics of their products

42. In their catalogs and in their newspaper and magazine advertisements, respondents have made statements and representations about the performance, efficacy and other characteristics of respondents' products. Seven products were specifically named in the complaint and allegations relating to false and deceptive representations were set forth in said complaint. During the discovery phase of this matter, complaint counsel attempted to use pretrial procedures to look into the efficacy of additional products. Respondents' objection to expanding this case in this manner was sustained and the issues on product performance, efficacy and other characteristics were limited to the seven products and the matters raised in the complaint.

JN INSTA-JET PROPANE FLAME GUN

43. In advertising their flame gun, respondents make the following representations (see CX 4 [1972]; CX 2 [1971]).

Fastest Way We Know To Clear Away Ice and Snow THE WORK-SAVER, THE HEART SAVER Lightweight, Easy-Handling New JN INSTA-JET PROPANE FLAME GUN [31]

> This new JN Insta-Jet Propane Flame Gun takes the work right out of dozens of clean-up chores. In winter, the adjustable instant-action flame clears away ice and snow faster than you'd believe possible. Whips through even the heaviest drifts. Clears walks and driveways . . .
>
> Produces a clean, hot flame for up to 14 hours on a single propane cylinder — easily obtainable at hardware, paint and department stores. . . .

The advertisements include a picture of a woman using the flame gun to clear a front walk from what appears to be a significant snow accumulation (see CXs 2,4).

In the complaint, it is alleged that respondents have represented that "The 'J-N INSTA-JET PROPANE FLAME GUN' is able to whip through the heaviest snow drifts and the thickest ice in seconds and is effective and efficient in clearing walks and driveways of ice and snow."

It is found that respondents have, in fact, directly or indirectly, made the representation as alleged in the complaint.

John Lomash, Sales Manager for the Engineering Division of the United States Testing Company (not affiliated with the United States Government) testified that when he was a Project Engineer he performed certain tests on a flame gun supplied by Gem Products Corporation (1238-9). At the time the test results were disclosed to the Federal Trade Commission, the consent of General Fabricators, parent company of Gem Products Corporation, was sought (1240). General Fabricators supplied flame guns to Norris in 1971-1972 (Stip. 38).[6]

On the basis of the tests, Mr. Lomash was of the opinion that the flame gun was not very effective in the removal of ice. The test revealed that it took 6.5 minutes to melt 1/8 inch of ice 1 square foot at zero degrees Fahrenheit, and 11 minutes to melt a 1/4 inch thick patch of ice one [32] square foot at zero degrees Fahrenheit (1251). In addition, they tested the maximum duration of the flame and found it would burn continuously at minimum length for 32 1/2 hours (CX 2481A, B).

Andrew Littlejohn testified that the flame gun he purchased from Norris in early 1973 was not effective in removing snow about 18 inches deep. He used it for about 45 minutes and "finally I got a hole down there where I could put my arms in" (342, 344). "It is no good for burning snow" (344).

Elliot Burger testified that when he received the flame gun from Norris, he purchased a propane cylinder and he assembled it. He tried to melt ice for ten minutes without success (603-4). He testified that the flame was not coming out of the end of the nozzle but out of the sides of the nozzle (614).

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[6] "Stip." refers to stipulation of counsel on the record during document day, the first day of adjudicative hearing in this matter. The numerical reference is to the page of the transcript on which the stipulation appears.

Frank Savoca purchased a flame gun from Norris in December 1971 (1492–3). He "received a long length of metal tubing, hollow tubing with a nozzle attachment at the bottom, with written instructions to obtain a propane tank at any hardware store" (1493). He further testified that the "ad gave the impression that the item was complete and ready for use" (*ibid.*).

He tried to melt off an "icy patch in front of the house" trying the gun on about "a square foot" patch for fifteen minutes. The result was "absolutely negative" (1494).

Respondents' representations as to the performance characteristics of their flame gun are total exaggerations. The flame gun will not "whip through even the heaviest drifts" of snow and is not "the fastest way . . . to clear away ice and snow." Moreover, it is not effective and efficient in "clearing walks and driveways of ice and snow." Respondents' representations are false and misleading.

The complaint further alleges that respondents have failed to disclose in their advertisements that the customer must purchase a propane gas cylinder and assemble the flame gun before it can be used. It is alleged that such facts are material to the consumers' choice of whether to purchase the product and that failure to disclose such facts constitutes a violation of the Federal Trade Commission Act. [33]

It is found that failure to reveal that the propane cylinder is not included, considered with the other representations in the advertisement (especially the picture of the person using a flame gun with a cylinder attached), is withholding a material fact.

The record is not clear whether the parts shipped do in fact come unassembled. Anyway, while it would be *nice* for everyone to know this fact, failure to disclose it is not, in the circumstances of the flame gun advertisement, a nondisclosure that would constitute an unfair or deceptive act or practice in violation of the Federal Trade Commission Act.

SURE-KILL ROACH POWDER

44. Respondents' advertisements on roach powder read, in pertinent part, (see CXs 17, 20, 23, 24, 25, 26; see also CX 117):

> Get Rid Of Roaches ONCE AND FOR ALL SURE-KILL WIPES OUT ROACH NESTS OR YOU PAY NOTHING
>
> Roaches can't resist Sure-Kill. They devour its odorless white powder and crawl to their nests, where they die. Then, a deadly chain reaction starts, that wipes out every

roach and every egg in the nest. Sure-Kill is safe to use, and never loses its killing power – even after years. A single can cleans out 6 to 8 rooms.

GUARANTEED ROACH-FREE FOR 5 YEARS Sure-Kill roach killer is guaranteed by the manufacturer to prevent reinfestation for up to 5 years when used as directed and left in place.

In the complaint it is alleged that through their advertisements on roach powder, respondents represent (Par. 10. (4–8)):

> Respondents' roach powder is safe to use.
>
> Respondents' roach powder gets rid of roaches once and for all. [34]
>
> Respondents' roach powder creates a deadly chain reaction which eliminates and kills roaches and eggs.
>
> The manufacturer has unconditionally guaranteed that respondents' roach powder prevents reinfestation when used as directed and left in place or it will refund money.
>
> Respondents' roach powder does not lose its capacity to kill under any conditions of use.

It is clear from merely reading the advertisements that respondents have made the representations alleged in the complaint.

Dr. Charles Mampe, Entomologist (relating to the "study of insects"), an employee of Western Industries, an "exterminating company," testified that he was employed for 10 years between 1964 and 1974 by the National Pest Control Association (1347–8).

He testified that boric acid is toxic to warm blooded animals, and used as a roach powder for the control of roaches in the home, it would represent a hazard (1351–2), if not used as directed (1390). He further testified that it was less effective than other products used, because it works much more slowly, approximately four days (1355, 1400). He added that he was not aware that any "chain reaction" occurs when boric acid is used as a roach control because the roach, to be killed, must contact and ingest the boric acid directly (1356). Although boric acid never loses its "killing power," for practical purposes, it loses its effectiveness if covered by dust or grease or becomes damp (1357). Boric acid will not be effective for five years under practical conditions (1359).

Dr. Mampe testified that, in his opinion, use of boric acid as a roach powder would not prevent "reinfestation," in the eyes of the homeowner (1365); that is because the presence of roaches moving from other places would appear in the places treated (1397, see 1407), and that the same is true for all roach controls (1410). He added that he was not aware of any information "that indicates that boric acid will kill roach eggs or in any way affect the eggs" 1366, 1380-1).

Boric acid has been used as a roach control since 1900 and it is effective in killing roaches (1352, 1391). It is not repellant to roaches (1401). [35]

Thomas Williams, inventor and manufacturer of Sure-Kill Roach Killer, testified that his product has been sold to Norris (1412, 1419). He testified that although he gives a money-back guarantee that the product will get rid of roaches, he does not use the words "wipe out" or "forever riddance" because roaches move around (1416-17; see 1423). He added that generally the product is effective for approximately six months (1423). He also testified that the "chain reaction" does not always happen and it is not the primary way of killing roaches (1424). He did not think that one application would be effective for 5 years (1425).

Mr. Williams testified that Sure-Kill was 50% boric acid, 50% inert materials (1435), was a good product[7] and that his money-back guarantee is unlimited as to time (1437). He also testified that, in his opinion, Sure-Kill was a safe product (1445).

Meyer Biddleman, President of Hye Test 303 Corporation, a manufacturer of chemical specialty products (1449), testified that his corporation compounds a roach powder for Valley Research Systems under the name High Action (1450). He drop-shipped this product directly to Norris between 1971 and 1975 (1450-1). This product is made of 50% boric acid and 50% inert ingredients (1451). He added that his customers like the product, "it does a terrific job" (1457, 1460). He guaranteed that the product would be effective and perhaps notified respondents that this guarantee was for a 5-year period (1463).

Edwin Meyer, President of Heddy Corporation, a manufacturer of chemical specialities, has sold a roach powder to Norris from 1973 (1475, 1479; see CX 2507). He never supplied Norris with any information about the efficacy of the product and has never discussed Norris' advertising with Norris (1484-5).

Emily Urf, the only consumer witness who testified about Norris' roach powder product, said that she ordered a can of that product in 1972, and that, after using it for [36] two months, she still had roaches (641-7, 654-5). She added that if she had known that the product was 50% boric acid and 50% inert ingredients she would not have bought it at the price she did pay (647-8, 653).

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[7] "It sure will kill the roaches if you put it in your home according to directions" (1441).

It is found that respondents' roach powder is relatively safe to use, if it is applied according to instructions (CX 2493C). The question is whether respondents' advertisements represent that the product is absolutely safe, *i.e.*, non-hazardous, and whether, as further alleged in the complaint, respondents' failure to disclose (1) that the product is hazardous, (2) that it may be harmful to human beings and pets, and (3) that special precautions should be taken in its use, constitutes misrepresentation in that such is a failure to disclose material facts to the potential consumer (see CX 4060, 4186).

In my opinion any overt representation that a potentially hazardous product is "safe" must be accompanied by a true statement as to the conditions under which it can be used "safely" (see CX 3020). Accordingly, respondents' unqualified representation that the product is "safe," is misleading, deceptive and unfair.

Respondents' roach powder is a formulation of boric acid which works slowly (CX 2493C). If used properly it will control and prevent reinfestation in treated areas. In many residential buildings cockroaches can move into the treated areas before those located there are completely eliminated. Accordingly, respondents' product may not get rid of roaches "once and for all," and respondents' unqualified representation that it does, is misleading and deceptive.

Respondents' roach powder will not kill roach eggs. Moreover, it does not create a deadly chain reaction which eliminates and kills roaches and eggs. Each cockroach must contact the boric acid to be killed. Accordingly, respondents' representations that the product creates a chain reaction and kills roach eggs are false and misleading.

Respondents' roach powder loses its capacity to kill roaches under certain conditions of use. If wet, it cakes and does not adhere to the roaches although upon drying it becomes an effective control once more (see CX 2493F). [37] If covered by grease or food deposits or dust, it becomes ineffective. Accordingly, respondents' representations that the roach powder does not lose its capacity to kill is false and misleading.

The record shows that the suppliers-manufacturers of the roach powder sold by Norris from 1970 to 1975 did unconditionally guarantee the product. There is no evidence that they did not honor this guarantee. The question is whether respondents' statement of the guarantee is, in effect, a representation that the product gets rid of roaches once and for all and does not lose its capacity to kill under any conditions. In my opinion, respondents' statement has the capacity to make such a false representation.

The complaint also alleges that failure to state the chemical ingredients (*i.e.,* 50% boric acid; 50% inert ingredients) is a failure to disclose a material fact. Boric acid is a well-known ingredient for roach killers. The consumer, who is ordering by mail, does not know what the ingredients are until receipt of the product. She is not in a position to make an informed judgment as to the nature of her purchase. Accordingly, facts as to the ingredients are material facts and failure to disclose them is failure to disclose material facts.

FOREVER SOCKS

45. Respondents' advertisements on socks read, in pertinent part, as follows (see CX 8, see CX 14):

> YOU'LL NEVER NEED TO BUY ANOTHER PAIR OF SOCKS AGAIN - FOR THE REST OF YOUR LIFE! (unless your laundry loses them).
>
> These revolutionary 8-ply socks are so indestructable . . . you can order Free replacements - pair for pair - for any you ever wear out . . . anytime!
>
> . . . Guaranteed to wear forever, in normal use. That "normal use" simply means don't burn holes in them deliberately, or try to cut them with scissors or razor.
>
> . . ."forever socks" . . .
>
> . . . "lifetime supply of socks"

The complaint alleges that by the above statements in advertisements respondents represented that their "Nylon socks" are "indestructable" and they "last forever" (Par. 10 (2, 3)). [38]

It is clear from merely reading the advertisements that respondents did *not* make the representations alleged in the complaint. What is represented is that these socks are *practically* indestructible and, if they wear out, the customer may order a free replacement from Norris. Accordingly, the advertisements present a "forever" guarantee, not an indestructible sock.

Robert Sharp, President of Sox Unlimited, selling agents for various Southern mills, testified that his company has been one of the suppliers of "hosiery to Norris for approximately ten years, off and on" (1504, 1515). He considered that the product "for wearability was a high quality sock, it is a heavy nylon sock" (1508). Neither the Southern mills (manufacturers) nor Sox Unlimited, guarantees the product (1511).

Mr. Sharp was of the opinion that the socks would not wear forever, and did not think "anything" was indestructible. However, he added that "they are good socks and they will last an awful long time" (1515), unless they are worn by a person with an oversized foot (1517, 1519-20).

Salvatore Marsala, the only consumer witness to testify about respondents' socks, said that he was attracted by respondents' statement in advertising that "you'll never need to buy another pair of socks again." He ordered a dozen pair, wore one pair a short time (one hour (595) or twelve hours (599)), and it developed a hole in the toe (595). They were returned to Norris (595).

Mr. Marsala testified that he had a shoesize of thirteen. As explained by Mr. Sharp, a shoe size of thirteen was actually an oversized foot for a thirteen sock size (see Sharp 1516-7; 1521-2).

Certain indirect representations not challenged by the complaint are that the manufacturers unconditionally guarantee the socks (see CXs 8, 14). In truth and fact, the manufacturers do not guarantee the socks. In any event, this area is outside the scope of the complaint and, in my opinion, it would be unfair to amend the complaint at this time to encompass these representations. The administrative law judge sustained respondents' objection to any further testimony relating to Mr. Marsala's return of the socks and any subsequent replacement or refund, as not being relevant to the matters for which the witness had been noticed to testify (595-7). There is no evidence that respondents do not live up to their own guarantee on the socks. [39]

FIVE YEAR FLASHLIGHT

46. Respondents' advertising on the "Five Year Flashlight" in pertinent part reads (CXs 44, 46; see CX 45, 2132):

THE FIVE YEAR FLASHLIGHT

Guaranteed Storage Capacity for 5 years or Your Money Back. 10 Times the Staying Power of an Ordinary Flashlight

* * * * * * *

. . . The completely new, Command Module 5 Yr. Flashlight

* * * * * * *

From the company that made flashlights for every manned Moon mission . . . Command Module Lighting . . . the flashlight with proved storage capacity for its power cell for AT LEAST FIVE YEARS combined with 10 TIMES THE STAYING POWER of any ordinary flashlight. Yours in a handsome Command Module case with no external switch to corrode or break . . .

* * * * * * *

ABSOLUTE 5-YEAR GUARANTEE

Every Command Module Flashlight carried this Absolute 5-year Guarantee. Carry your flashlight with you, keep it at home. It must work even if you haven't touched it for 5 years or your money back. So don't be another minute without the one safety element every car, every family needs.

It is alleged that through their advertising respondents represented that their "five year flashlight" carries an absolute 5-year guarantee (Par. 10 (13)). From a reading of the text of the advertisement, including the "guarantee" as described in the advertisement, it is clear that Norris did make the representation alleged in the complaint.

Chromalloy Electronics supplies the battery to Norris (RX 7, 8). Its guarantee to the consumer reads as follows (CX 2044B; Stip. 811-12):

Your 5 Year light is guaranteed against defects in materials and workmanship for a period of 30 days. [40]

If, during the 30 day period, your light fails to operate . . . return it to the dealer for an immediate exchange.

Your light is also guaranteed to remain usable for a period of five years providing it has not been used more than 10 hours. Specifically, the light is guaranteed to store and remain useable for 5 years or operate for a total of 10 hours, which ever comes first.

In the event that the light does not work and has been used for less than 10 hours and is less than 5 years old, return the light (prepaid) with proof of purchase and date of purchase to the address below for battery analysis and replacement.

Proof of date of purchase is considered to be the burden of the consumer and each proof must be supplied when applying for guarantee replacement.

Guarantee valid only during normal care and use at ambient temperatures. Abuse of the light or tampering with the case voids the guarantee.

The foregoing is in lieu of all other guarantees, expressed, implied or statutory and Chromalloy Electronics neither assumes or authorizes any person to assume for it any other obligation or liability in connection with the sale of this product.

Counsel also stipulated, and David Rush, President of ACR Electronics, Inc. (formerly Chromalloy) (811), agreed that if he testified he would state that "the average amount of time that the ordinary person would normally use or generally use a flashlight, any flashlight, would not generally exceed two hours per year" (Stip. 813).

In the instructions to the consumer, Chromalloy advises in pertinent part (CX 2044A):

This unique light was designed primarily for emergency use. It is the only light that can be left in your kitchen drawer or car glove compartment for a period of 5 years and still operate.

> Of course the light will not stay "on" continuously for 5 years but with normal emergency type use, it will retain its power for the full 5 year period. The total "on" time of 10 to 20 hours means a minimum of 4 half hour emergency uses each year for 5 years. [41]
>
> Simply stated, the light will not self destruct like all other lights.

Clara Zappa, the only consumer witness who testified about the Norris flashlight stated that after three months, during which she checked to make sure it was in working order, "it was not a flashlight any longer . . . [i]t seemed to be dead" (533).

Norris' "Five Year Flashlight" is guaranteed by the manufacturer to store and remain usable for 5 years or to operate for a total of 10 hours, whichever comes first. The manufacturer further clearly states in its guarantee that the light will not stay "on" continuously for 5 years. Respondents' representation that the flashlight carried an absolute 5 year guarantee is false and misleading.

It is further alleged in the complaint that the facts that (1) the flashlight has an "on" life of 10 to 20 hours, and (2) the manufacturer guaranteed that the light can be stored and remain usable for 5 years or operate for a total of 10 hours, whichever comes first, are material facts and that respondents' failure to disclose those facts was a violation of the Federal Trade Commission Act (Par. 12).

Considering the content of respondents' advertisements, it is found that the facts alleged to be material are important to the consumers' decision as to whether to purchase the product, and that respondents' failure to disclose that information is unfair and has the tendency and capacity to mislead the purchasing public.

LINCOLN-KENNEDY PENNY

47. In their advertisements for the "Lincoln-Kennedy Penny" respondents state in pertinent part (CX 69, see CXs 62, 66, 275):

> Now Available WORLD'S FIRST LINCOLN-KENNEDY PENNY –
>
> UNCIRCULATED COMMEMORATIVE LINCOLN HEAD PENNY WITH KENNEDY PROFILE
>
> * * * * * *
>
> Here's unusual news for collectors and anyone interested in unique commemorative issues . . . issues that may never be repeated again. A new, uncirculated Lincoln Head penny is now available. [42]
>
> This unique coin shows the profile of President Kennedy stamped on the surface, looking at President Lincoln. The relationship is uncanny. Never released through ordinary channels, the coin is perfectly legal tender, acceptable under section 33[1], Title 18 of the U.S. Code. As a coin of both historical and numismatic significance, it

might well become a sought-after collector's item that could grow and grow in value. Because, however, this coin is not in circulation, you may obtain it only through an offering of this sort, and we urge you to order now, avoid disappointment. And if you order right away, you will also receive The Plaque of Coincidences, showing the startling parallels in the careers of these two tragic figures . . .

FREE WITH EACH COIN ORDER HISTORICAL RESUME OF ASTONISHING COINCIDENCES BETWEEN LINCOLN & KENNEDY

* * * * * * *

These and many more astonishing coincidences are yours in your Free Plaque of Coincidental Facts when you order the Lincoln Kennedy Commemorative Penny.

The complaint alleges that through such advertisements respondents represent that (Par. 10 (24, 25, 26, 27)):

1. Respondents' Lincoln-Kennedy penny was minted by the United States Treasury Department;
2. Respondents' Lincoln-Kennedy penny is a coin of historical and numismatic significance which is certain to grow in value;
3. The issuance of respondents' Lincoln-Kennedy penny was sanctioned by Section [331], Title 18 U.S. Code; and
4. A free plaque containing historical coincidences between the lives of President Lincoln and President Kennedy is provided to purchasers with each coin.

From a reading of the advertisement as a whole, and with special attention to the statements quoted above, it is clear that respondents made the representations as alleged in the complaint. [43]

Norman Stack, a rare coin dealer with 30-years experience, testified that a "Lincoln-Kennedy Penny does not exist as struck by the United States Government," and that its existence is not unusual news for collectors (1322). He was of the opinion that altering an already minted coin does not increase its numismatic value, which is determined because of a shortage of the coin, by attrition or by the quantity struck (1326, 1331, 1341-2, 1344). He added that the Lincoln-Kennedy Penny, because it was not struck by the United States Mint was of no historical significance, was not of numismatic significance, was not a "commemorative coin" and was never "minted" (1332).

Henry Weissblatt, former President of Federal Coin and Currency, a gold coin wholesaler, and a coin dealer on his own, testified that the so-called Lincoln-Kennedy penny shown to him was not "unique," was not minted by the United States, was not unusual news for collectors, was not of numismatic significance, and was not a commemorative coin (1468-9). He added that, in his opinion, the coin would not be of value to coin dealers (1470).

On August 1, 1973, the United States Postal Service, by its General Counsel, initiated a proceeding wherein it was charged that respondents, in advertising its "Lincoln-Kennedy Penny," had made false representations (CX 3029):

1. That the United States Treasury Department has minted a commemorative Lincoln Head penny with a Kennedy profile;
2. That the Lincoln-Kennedy penny, though legal tender, is uncirculated and never released for ordinary use;
3. That the issuance of the Lincoln-Kennedy penny is sanctioned by Section 331, Title 18, U.S. Code; and
4. That because said coin is of historical and numismatic significance, it is certain to become a collectors' item that will grow and grow in value. [44]

Chief Administrative Law Judge Duvall, in his initial decision filed October 19, 1973, found that respondents had made the representations alleged in the Postal Service complaint. He also found that representations 1, 3, and 4 were false, but found that the second representation, although technically false, was not "a material misrepresentation" (CX 3030).

The Postal Service, in its opinion filed February 27, 1974, sustained the administrative law judge's findings as to 1 and 4, and indicated that it believed determination as to the material nature of representation 3 was covered under its findings as to representation 1 (CX 3032). The Postal Service determined that respondent Norris was engaged in a scheme or device for obtaining money or property through the mail by means of materially false representations, and issued, on February 27, 1974, through its Judicial Officer, an order relating to the limited postal services thereafter available to Norris. Subsequently, the parties stipulated as to the handling of Norris' mail which was approved on March 12, 1974, by the Judicial Officer (CX 3034).

The particular representations challenged in the Federal Trade Commission proceeding appear to be similar to those considered by the Postal Service and those advertisements were disseminated before the issuance of the Postal Services' Order.[8]

It is clear that the Lincoln-Kennedy penny was not "minted" by the United States Government and that issuance of the Lincoln-Kennedy penny was not sanctioned by Section 331, Title 18, U.S. Code. Only the Lincoln penny, on which the Kennedy profile is superimposed, was minted and sanctioned, and respondents' representations are false and misleading.

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[8] Advertisements disseminated after the Postal Service order are CX 275 (February 9, 1974) and CX 405 (at page 11, 1975 Catalog).

The Lincoln-Kennedy penny is of no historical and numismatic significance and there is no indication that it is certain to grow in value. Respondents' representations in this respect are false and misleading.

Finally, respondents offer of a FREE plaque (see CX 3027) is actually not an offer of a "free" item. The plaque is part of the [45] regular offer at the price of the coins and plaque, and accordingly the use of the word "Free" is unfair and deceptive.

TV ANTENNA

48. In advertisements for their "JUMBO TV ANTENNA," respondents make the following statements (CXs 28, 886 (p. 46)):

> Every home a super receiver ELECTRONIC MIRACLE TURN YOUR HOUSE WIRING INTO A JUMBO TV ANTENNA
>
> Do you know that you have one of the greatest TV antennas ever constructed? It's better than any set of rabbit ears, more efficient than complicated external antennas. It's your house. Yes, the wiring in your home constitutes a giant antenna that acts as a super receiver for TV, FM, all kinds of difficult reception.
>
> And the secret to using all this reception potential is an amazing little plug-in attachment that utilized the receptivity of your house wiring without using a single bit of electrical power. Yes, you simply attach the adapter easily & quickly to your set . . . plug it in to any wall outlet and immediately your entire electrical system is working for you. No ugly looking rabbit ears, no difficult, dangerous to maintain external antennas, and reception so sharp and clear it will amaze you even in the more difficult areas.

In the complaint it is alleged that through their advertisements respondents represented that (1) the TV antenna will bring sharp and clear reception even in difficult areas; (2) the performance of respondents' TV antenna is superior to any rabbit ear antenna or outdoor antenna; (3) respondents' TV antenna will turn all types of house wiring into a TV antenna; and (4) respondents' TV antenna is an electronic miracle (Par. 10 (9, 10, 11, 12)). [46]

From merely reading the advertisements, especially the portions quoted above, it is clear that respondents made the representations set forth in the complaint.

Frank Triolo, an electronics engineer employed by the United States Electronic Command in Fort Monmouth, New Jersey, testified that he conducted tests on the Norris TV antenna ("C-M Antenna") in December 1973, at the request of the Federal Trade Commission (272-3). From a comparison of the actual pictures received on television sets as well as an electronic measurement of the "received voltage" at the television sets, Mr. Triolo concluded that the Norris antenna was "definitely inferior to all the other antennas that we used for comparison" (275; CX 2704).[9]

Mr. Triolo was of the opinion that the performance of respondents' TV antenna was not superior to any rabbit ear antenna or outdoor antenna and that it was not an electronic miracle (327-8). He testified further that house wiring can be turned into a TV antenna, although a poor one (328).

Frank Trupia testified that he purchased a TV antenna from Norris in 1973, and that the picture he received with that antenna was inferior to the picture received with the antenna he already had. He added that the television picture with the Norris antenna "was not even good" (332, 335).

Leonard Scrudato testified that he purchased a Norris antenna and "wired it up as I was instructed, and the performance was nonexistent" (469).

Respondents' presented an affidavit and it was stipulated that they had received a communication from a customer expressing satisfaction with the performance of Norris' TV antenna that they had purchased (RX 9AB; Stip. 1821-2).

It is found that respondents' TV antenna will not in all instances bring sharp and clear reception in difficult [47] areas and is not superior to rabbit ear antennas and outdoor antennas and respondents' representations in this respect are false and misleading. Respondents' antenna is not an "electronic miracle" and respondents' representation that it is, is false and misleading.

Respondents' representation that their TV antenna turns the house wiring into an antenna is true. There is nothing in the record to demonstrate under what conditions, if any, utilization of house wiring is ineffective and accordingly respondents' representation has not been shown to be false and untrue.

EX-TAXICABS

49. In their advertisements for cars, respondents[10] made the following statements (see CXs 53, 58; see CX 50, 51, 56):

> BUY CHOICE . . . NOT CHANCE
>
> Buy direct and get the carefully maintained car of your choice below wholesale price
>
> All cars are standard four door, six passenger sedans equipped with automatic

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[9] CX 2704, p. 4: "CONCLUSIONS": The C-M Antenna is definitely inferior to the conventional home and "rabbit-ears" antennas used in these tests. It does not serve as an effective TV antenna system in the suburban and fringe areas in which it was tested.

[10] In finding 49 the term respondents refers to Norris, Pan-Am, Jacobs, Williams and Kenneth Mann.

transmissions, heater, defroster and feature durable vinyl interiors. They have been in regularly maintained fleet use and serviced far more frequently than the average car owner can afford to do. Each car has been thoroughly serviced by our mechanics to put it in good operating condition and passes careful inspection before being released for delivery. These top-quality ex-taxis have been carefully selected for best value . . . .

We offer these fine cars at the prices shown (F.O.B., N.Y.). There are no hidden costs! . . . (CX 58).

IDEAL FOR PERSONAL USE OR TO RESELL AT A PROFIT

ONLY PAN AM GIVES YOU THIS 100% O.K.

Dependable PAN AM gives you a good car at a low price. Our highly trained mechanics double-check each car for all the items below. When a car leaves our premises it is checked out as follows: [48]

Brakes
Plugs
Points
Lights
Battery
Fan Belt
Spare Tire
Jack
Transmission
Heater
Defroster
Generator
Starter
Water Pump
Fuel Pump
Block
Color

MAIL THIS COUPON WITH YOUR DEPOSIT — ORDER AS MANY AS YOU WANT
ALL CARS ARE SOLD ON AN AS IS FIRST ORDER — FIRST SERVE BASIS

In the complaint it is alleged that through their advertisements, especially the statements quoted above, respondents have represented that (Par. 10 (14-23)):

1. cars delivered to purchasers are in good mechanical and physical condition;
2. cars delivered to purchasers are in safe operating condition;
3. cars delivered to purchasers are finished and look as pictured and described in respondents' advertising;
4. cars are checked by expert mechanics and necessary repairs are made prior to release for delivery;
5. cars delivered to purchasers are in sound condition and repair and render normal, adequate and satisfactory service;
6. respondents' cars may be readily resold by the purchasers at a profit;
7. cars are regularly ordered and received in advance of their being offered for sale and are held in stock until purchasers' orders are received;
8. respondents' cars have undergone thorough and complete servicing and inspection before being released and approved for delivery;

9. each price quoted for respondents' motor vehicles is the full price and there are no hidden costs; and

10. respondents bear the liability and responsibility of delivery of cars to purchasers at any destination in the United States where such purchasers may reside. [49]

From a reading of the advertisements in their entirety with special attention to the excerpts set forth above, it is found that respondents do make the representations alleged in the complaint.

Almost all, if not all, of the cars sold by mail-order by Pan-Am were supplied to it by Future Motors. These cars were trade-in taxis from some twenty taxi fleets located in the New York City area. Respondent Mann testified that between 1969 and 1974, Future Motors sold a total of approximately 700 to 800 ex-taxis to Pan-Am, (Mann 214).[11]

After the cars were sold to Pan-Am, Future Motor's personnel serviced them. The service ordered by Pan-Am appeared on service order forms (see RX 32A-I). After such services were performed, the ex-taxis were painted, and "new" tires were installed by Future Motors. These services by Future Motors were performed either before or after the customer-purchaser was known to Pan-Am.

For consumers located in New York State, a State Inspection Certificate was required in order to secure State License application forms.

Ten consumers who had purchased cars from Pan-Am testified about their ordering and the delivery as well as their experience with their cars.

Patricia Berardi, a New York State resident, testified that in 1972 her husband purchased a 1970 Dodge Coronet for $700, ordering by mail from Pan-Am (1131-4). They knew that it was an ex-taxi (1135, 1139). In describing the appearance of the car that she received, Mrs. Berardi said:

> The car looked good. Mine happened to be a turquoise color, a nice color green.
>
> The tires looked fine. The car was clean on the outside. It was very dirty in the inside . . . (1138).

She further testified that she had the car ten months. About three months after her car was delivered she had trouble with a loose bolt on the steering box. She returned to Future Motors (at College Point) about four months after she picked it up to have the steering box repaired and, although the [50] personnel there worked on the car, the problem was not solved. She had it repaired at a neighborhood station.

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[11] Pan-Am ceased operations in 1974; only a relatively few car sales were made in that year (Mann 212).

Six months later she experienced trouble starting the car, and a neighbor replaced a "solonoid switch" inside the starter (1141). She also installed a muffler (1141). Thereafter she experienced difficulty with the transmission, "it just wouldn't go into reverse." She gave "it to some friends of my husband for the parts."

Catherine Dyshuk, resident of Scranton, Pennsylvania, testified that in 1972 she and her husband, responding to an advertisement in the Norris catalog (1221), ordered a 1971 Dodge Coronet by mail from Pan-Am for $999 (1214). Her husband, beginning in August, made three trips to New York to pick up the car. He was not successful. On December 17, 1972, the car was delivered to the Dyshuk home (1215). Mr. Dyshuk signed a receipt stating that it was received "in good condition" (1227).

Concerning the appearance of the car, she testified that the paint was already coming off. They did not know they were getting a taxi (1216), but thought they were getting a "fleet car" (1223). The next day they took it to a mechanic who showed them the bent frame of the car and some "dents in the side" (1217-8). She did not drive the car more than twice. Her husband drove the car to work for six months (1219). Then they sold it for $100 (1220).

In early 1972, when Steven Fuchs was a resident of Demarest, New Jersey, he purchased a 1969 Dodge Coronet for $599 from Pan-Am, responding to an advertisement in a Norris catalog (750-1, 755). From his interpretation of the advertisement he thought he would get a "reconditioned fleet car or taxi." "The advertisement portrayed a car which looked to be brand new, and I assumed the car would be reasonably well restored, and it said it did have new parts, and I remember it saying new tires, which is important, and a new paint job as another thing" (752).[12]

Mr. Fuchs picked up the car at College Point, after paying for it at the Norris office in Freeport (753).[13] He test drove the car and told the personnel at College Point that the "brakes barely worked" (753). The car [51] was serviced and "the brakes were a little better but they weren't what I considered safe, but I took the car." (753). "[T]he paint job was totally inadequate." "I noticed that the headlights were not focused. One was facing up and one was facing down, it was loose. The emergency brake didn't work" . . . (753). He was of the opinion that the tires, which looked new, were "retreads" (769–70).

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[12] Mr. Fuchs understood the phrase "as is" to mean "the way you receive it" (759).

[13] The invoice signed by Mr. Fuchs reads: "Above car approved and accepted. No warranty expressed or implied" (CX 42 32).

He kept the car for a couple of weeks and then returned it to Pan-Am and received his money back (755, 758).

John Kurimski, a resident of Stratford, Connecticut, purchased a Dodge car by mail-order in 1971 from Pan-Am for $1000 (1173–4). About six months later the car was delivered to the Kurimski residence in Stratford (1178). He paid the driver $50 (1178). He signed a statement that it was in "good condition" (1186).

Mr. Kurimski had the car for "approximately a year or so, but that thing just stayed in the driveway" (1183). "I don't think I had gone more than a hundred miles" (1183).

As to the kind of car he expected to receive, Mr. Kurimski testified as follows (1183):

> Paint color you wanted, blue or red I think it was, something like that. It sounded good, that's why I got it, but I also expected to be able to make repairs on the car because when you get a used car, naturally there is always some work to be done. You don't get in a condition that good, but not to the extent that when I looked at this thing, what it was going to cost me. This was a piece of junk, period.

He further testified that although the paint job was pretty good, the interior was "a mess" (1178). "The engine was bad, all rusted out." He "tried to get the car going. It wouldn't go, kept stalling." He had it towed to a garage. They "found that the main bearings were gone." They got it going and then on the eight-mile trip home it stalled about ten times (1179).

He and a friend, who was a mechanic, replaced one bearing and found the frame broken and welded. "[T]he [52] weld job was terrible" (1180).[14] In addition he replaced the points, plugs, condenser and timed it, replaced the front ball joints, muffler and carburetor (1182). The total cost of repairs was approximately $300 to $400 (1181).

Mrs. Truus M. Lamanna, a resident of East Norwich, New York, testified that in 1972 they purchased a 1970 four door [Dodge] Coronet from Pan-Am for $700, responding to a catalog advertisement (1098–9; see RX 4). From the ad, they thought a 1970 car should be a pretty good car, being a fleet car which would be constantly serviced, it should be in good condition (1100).[15]

She paid for the car in Freeport and picked it up at College Point at Future [Motors]. She had to go to College Point twice because on the first visit the car "hadn't been inspected yet" (1102). "It had a new paint job, only the outside, because when you opened the trunk it was still all yellow, and the upholstery was taped up where the mechanism for the cab had been attached" (1102). "The inside was very dirty" (1102).

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[14] Mr. Kurimski is a welder (1181).

[15] The Lamanna, Lo Motto and Berardi cars were bought as part of one transaction (see 1107). Down payment with the order was made on April 12, 1972, the balance paid July 13, 1972, and the cars were picked up on July 27, 1972 (1109, 1111).

From the following day she had trouble starting the car, the "starter solonoid" being defective (1102). Within three months "the tires were completely shot, the front" (1104). "One day my whole front went, the whole "A" frame ["K"; see 1109-10] collapsed" (1104).

They had it towed back to College Point, and after two months she got her car back (1105). Six months after picking up the car the first time (late August) she gave the car to some kids "experimenting how to fix cars" (1105).

Upon receipt of the car she signed a statement: "Above car approved and accepted. No warranty express or implied. Any major thing go wrong, may be brought back, repaired at Pan-Am expense" (1111). [53]

Willie Lewis, a resident of Capitol Heights, Maryland, ordered two cars from Pan-Am by mail (1022). In March 1972, he ordered a Dodge Coronet for $699, receiving delivery in June at College Point (1024; see CX 3211). In June he ordered a blue 1970 Dodge Coronet for his wife and picked it up in October (1037). He signed a statement: "Above car approved and accepted. No warranty express or implied" (1052).

In his view the advertisement (CX 55A) to which he responded represented that the cars were "inspected, they were in condition, . . . and guaranteed for thirty days . . . they were very reliable" (1023, 1047). He "expected to receive a car which had been used, but I expected to receive a car that would give me service, adequate service, for a certain length of time without any trouble." Although he knew they were "used" "fleet cars," he didn't see anything in the advertisements about ex-taxis (1044).

While he was driving the first car home, the "lights went out." In July he replaced the "disc brakes" (CX 3212) and later the power steering failed (1030-1). Pan-Am reimbursed him $50 of the $150 cost of repairing the power steering (1032).

In the spring of 1973, the motor blew up and he had that replaced for approximately $300 (1033). He further testified that on the first day he noticed that the voltage regulator was defective (1034). Thereafter he carried a spare generator in his car (1035), and replaced the generator every six months (1035). In the latter part of 1973, he junked that car.

He had to replace the front end of the second car (CX 3218) and sometime later "one night I was driving it home and, all of a sudden, whoof, the whole dashboard caught fire" (1039). He had other "troubles, minor, but I was able to repair them myself" (1043).

Frank LaManto, a resident of South Farmingdale, Long Island, New York, picked up a 1970 Dodge Coronet in late September 1972 (1118). It was "in a condition of a brand new painted car, a brand new-looking painted car from the outside." The interior "was a little disappointment, but it was still satisfactory" (1118-9). The car had an inspection sticker on it (1119). He signed an invoice dated August 1, 1972, which stated: "Above car approved and accepted. No warranty express or implied" (1129). [54]

He drove it home and noticed a problem with the transmission. The next day he returned it to College Point, where a used transmission from another cab was installed (1120). Approximately four months later the "engine seized" (1121).[16] He replaced the motor four months later at a cost of approximately $600 (1123). Three months later the car developed trouble in the drive train. They sold it for $700 in July 1976 (1125). The car was driven 6000 miles during the seven months it was in running condition (1125).

Carol Orkin, a resident of North Babylon, New York, purchased a 1970 Ford for $700, responding to an advertisement in the Norris Catalog (1059-61). She ordered it in July 1972 and picked it up in February 1973 (1063). From the advertisement "it was reasonable and it was a new car, comparatively. It was only two years old, and I thought it would be a good buy" (1061). "I knew I was buying a fleet car from the advertisement, but I assumed that since it was a fleet car it would be kept up properly . . ." (1062, see 1086).[17] When Mr. and Mrs. Orkin picked up the car it had an inspection sticker on it (1065). On the way home they stopped at a gas station because there were "no brakes on the car." A "master cylinder" was put in the car by the station attendant (1066). She requested a refund on that bill from Norris, but never got a response from them (1072). They kept the car for about a year and finally "resold it to a junkyard for $35.00" (1072).

Charles Weyland, a resident of Freeville, New York, purchased a 1972 used Dodge Coronet from Pan-Am for $999 plus tax (1155–7). He picked up the car at College Point in March 1974. It had an inspection sticker on it (1157). To the best of his recollection he did not see "ex-taxis" in the advertisement (1166).

He drove the car from College Point to a nearby gasoline station to get gasoline. The car failed to restart. The gas station secured the positive terminal of the battery (1158). Shortly after he continued his trip home, the brakes on the right front "seized" (1158). He returned to College Point, [55]

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[16] "It's a condition that happens when the engine runs completely out of oil and there is nothing to indicate that" (1121).

[17] They were aware that fleet car may mean ex-taxis (1087).

The service people at College Point replaced the battery and the front brakes and bearings, obtaining parts from other cabs, as well as a hanger on the exhaust pipe or muffler (1159).

On the way home the car overheated. The radiator had to be flushed out and the anti-freeze replaced (1160). Shortly thereafter they discovered a hole in the floor board (1160). He had further front brake trouble and had to have the "spider gears" replaced (1161). The paint started to peel in 1975 (1163). They gave it to a dealer to resell (1163).

George Roberts, a resident of Springfield Gardens, New York, ordered a car by mail from the Norris catalog for $795 (713–4). He picked it up in May 1970 (715). He testified that if he had known it had been a "taxi," he would never have invested or decided to buy it (7160). The service people attached an inspection sticker to the car while Mr. Roberts was signing papers (717).

Upon driving it away, Mr. Roberts discovered that the brakes didn't work. He backed it to the College Point service area and they adjusted the brakes (718).

Two and a half months later he was stopped by a policeman for having an invalid inspection sticker on the car. Because it would require $300 repairs to get a valid inspection sticker, Mr. Roberts sold the car to the mechanic at the inspection station for $75 (721).

In a number of instances, cars delivered to purchasers are not in good mechanical condition and respondents' unqualified representation that they are, is false and misleading.

In a number of instances, cars delivered to purchasers are not in safe operating condition, and respondents' unqualified representation that they are, is false and misleading.

In a number of instances, it appears that the cars have not been serviced and necessary repairs had not been performed before release for delivery and respondents' unqualified representation that inspection, service, and repairs are performed in advance of delivery is false and misleading. [56]

In a number of instances, cars delivered to purchasers are not in sound condition and repair and have not rendered normal, adequate and satisfactory service. Respondents' representations as to the condition of the cars they sell is false and misleading.

In a number of instances respondents' cars have not undergone thorough and complete servicing and inspection before being released for delivery and respondents' representation that such servicing and inspection is always performed is false and deceptive.

It appears that in many instances the cars ordered by customers by mail are not in stock, but are obtained as available to fill orders. Respondents' representation that they are offering for sale cars that are in stock is false and misleading.

It appears that all of respondents' cars are not in such condition that they may be sold at a profit by the purchaser. In many instances purchaser had to expend substantial sums of money in repair costs. Respondents' unqualified representation that such profit may be realized is false and misleading.

Respondents' cars are repainted on the exterior before they are delivered to purchasers. Generally, the appearance of the cars was as pictured in the catalog advertisements. However, the interiors are not refinished. There is no overt representation that they have been so serviced. Respondents' have not misrepresented the *appearance* of the cars which they sell.

Each price quoted for respondents' cars is the full purchase price except for the tax (for New York residents). The delivery charge for delivery to the purchasers' home is stated in the advertisements. Except for the necessary repairs that a customer might be required to make, there are no hidden costs. In my opinion, the "hidden costs" refer to the original price and not to subsequent repair costs, and respondents have not misrepresented the purchase price of their cars.

There is no evidence as to who bears the liability and responsibility of delivery and accordingly there is no proof that respondents' representations that they do, is actually false. [57]

It is further alleged in the complaint that respondents have failed to make known to the prospective purchaser certain material facts about their cars.

First, it is alleged that respondents do not disclose that the cars are "ex-New York City taxicabs." In their advertisements, respondents do state that their "fleet cars" are "ex-taxis." The additional disclosure that they are ex-New York City taxicabs is a material fact and failure to make this disclosure is unfair and has a tendency and capacity to mislead the prospective consumer.

Second, it is alleged that respondents advertise that their cars are sold "FOB New York" and "As is," without disclosing the meaning of those terms. There is no evidence that respondents have made any representation that their cars are sold on other terms. Absent some ambiguity, sellers are not required to define words that have well-known and particular meaning.

Third, the complaint alleges that respondents do not disclose that the cars are not inspected for compliance with any state motor vehicle inspection law. The record discloses that the cars sold to New York State residents have inspection stickers attached thereto. There is some ambiquity in the advertisements as to what "inspection" is represented as having been performed. It would appear that state law covers the inspection requirements and to require further disclosure in advertisements would create more confusion as to what is actually a fact.

Fourth, the complaint alleges that the interiors of respondents' cars have not been cleaned or reconditioned prior to being delivered to the purchaser. In fact, it appears that the interiors are not reconditioned. This is a material fact and failure to disclose it, especially in view of the other representations relating to the condition of the cars, is unfair and had a tendency and capacity to deceive.

Finally, the complaint alleges that respondents have failed to disclose that the drivers hired to deliver cars to purchasers are independent contractors and are not respondents' agents, servants or employees. The record does not demonstrate that failure to make this disclosure is important. There does not appear to be any serious ambiguity in the advertisement that would require this disclosure, and it is found that any such fact is not material to the purchasers' choice of whether to buy respondents' cars. [58]

DISCUSSION

About respondents' liability

The acts and practices challenged in this proceeding are primarily the acts and practices arising from the business operations of corporate respondent Norris. It is clear that respondents Jacobs and Williams are responsible for these acts and practices in their individual capacities, as well as corporate officials, for purposes of enforcement of Section 5 of the Federal Trade Commission Act. They control the policies of the corporation and direct its operations. See *Standard Educators, Inc.* v. *Federal Trade Commission,* 475 F.2d 401 (D.C. Cir. 1973), *cert. denied,* 414 U.S. 828; *Guziak* v. *Federal Trade Commission,* 361 F.2d 700, 704 (8th Cir. 1966), *cert. denied,* 387 U.S. 1007 (1965).

None of these general practices are attributable to Pan-Am or Kenneth Mann. The only business that they are engaged in is the mail-order business of selling used cars. Of course, respondents Jacobs, Williams and Mann are responsible individually and as corporate officers for the acts and practices of Pan-Am. *Federal Trade Commission* v. *Standard Education Society,* 302 U.S. 112 (1937).

The other two corporate respondents had nothing to do with the challenged practices. Complaint counsel concede as much (CSC PF pp. 47–48). Without further discussion, the complaint will be dismissed as to the two corporate respondents Federated Nationwide Wholesalers Service, Garydean Corp., t/a Nationwide Wholesaler Service, and P-N Publishing Company, Inc.

The only remaining question as to respondents' responsibility for the challenged acts and practices is the relationship between Norris and Pan-Am. Although it was conceded that Norris was not in the business of selling cars (see tr. 66), the advertisements of Pan-Am appeared regularly in the Norris catalog and Pan-Am's business was conducted by Norris personnel at the Norris place of business (see Cxs 752–54, 756). In the circumstances, the practices of Pan-Am which arose out of advertisements in the Norris catalog (see CXs 57, 409, 410) are found also to be the responsibility of Norris, for purposes of enforcement of the Federal Trade Commission Act. See *Sunshine Art Studios, Inc.* v. *Federal Trade Commission,* 481 F.2d 1171 (1st Cir. 1973). [59]

About the Commission's jurisdiction

There is no dispute that the Federal Trade Commission has jurisdiction over the respondents Norris, Pan-Am, Jacobs, Williams and Mann. They are engaged in commerce within the meaning of the Federal Trade Commission Act, and the challenged acts and practices are in commerce and affect commerce within the meaning of that Act.

Meaning of the advertisements

With several exceptions, it has been found that the advertisements conveyed the meanings set forth in the complaint. This determination has been made from carefully considering the advertisements, including the format and the emphasis placed on certain words and phrases contained therein. It is well established that the meaning of an advertisement may be determined by an examination of the advertisement itself. *Carter Products, Inc.* v. *Federal Trade Commission,* 323 F.2d 523 (5th Cir. 1963); *J. B. Williams Co., Inc.* v. *Federal Trade Commission,* 381 F.2d 884 (6th Cir. 1967).

Such a determination may be made notwithstanding that the advertisements may have other meanings. Implications and inferences may be made from statements actually made as well as from information not set forth therein, if the excluded facts are material, *i.e.,* facts considered to be material to the customers' choice whether to purchase the product advertised. *Chrysler Corp.* v. *Federal Trade Commission,* D.C. Cir. decided July 6, 1977 slip opinion at p. 12; *Federal Trade Commission* v. *Colgate-Palmolive Co.,* 380 U.S. 374 (1965).

Respondents do not seriously contest the issues as to whether the challenged advertisements conveyed the alleged meanings. They do point out that with respect to the FLAME GUN advertisements the words "in seconds" do not appear therein, and argue that the alleged meaning which contains "in seconds" should not be interpolated from the advertisement (Resp. PF pp. 27-28). This advertisement uses such phrases as "fastest way we know" and "faster than you'd believe possible." Speed of performance is the theme. That is close enough.

About the performance characteristics of products

Respondents argue that complaint counsel have not proved that the performance characteristics of the products [60] are not as represented so as to render the challenged advertising false, deceptive or misleading in violation of the Federal Trade Commission Act.

With respect to the FLAME GUN, respondents argue that the test conducted by Mr. Lomash was limited to two one foot square sections of ice at zero degrees (0°) and that his test did not duplicate the environment or conditions which an ordinary consumer might encounter (Resp. PF pp. 30-32). In respondents' view the testimony of the three consumer witnesses should be disregarded because they were not competent to testify as to the technical or scientific validity of the claims made for the product and that they had no way of knowing whether the units they were using were not defective (Resp. PF pp. 28-29).

In my opinion the evidence of record is competent to support the finding that the FLAME GUN could not perform as represented in the advertisement. The burden shifted to respondents to come forth with some information in support of their claims. They did not do so.

The same situation exists with respect to the TV antenna. The test conducted by Mr. Tripolo at least demonstrated that the TV antenna did not produce the results as represented in respondents' unqualified advertisements. The fact that the TV antenna may have worked, as promised, in certain other areas of use, does not make the unqualified representation truthful as to all possible consumers.

As shown by the findings on the other products' performance characteristics, respondents' representations were to a great extent exaggerations or statements of true facts in a way that they had a tendency and capacity to mislead. In my opinion complaint counsel have sustained their burden of proof and without rebuttal evidence the record is sufficient to support these findings.

About general practices relating to the mail-order business

One of respondents' principal defenses to the allegations relating to nondelivery of merchandise and their failure to make prompt refunds centers around the relatively few complaints attributed to them compared to the great number of orders they process every year. Contending that the [61] complaints are inconsequential in terms of respondents' overall volume and operation of its business, respondents assert that the evidence offered herein by complaint counsel, involving a relatively minute percentage of the consumers which the company must deal with on a day-to-day basis, does not rebut the evidence of respondent Norris and its officers as to the policies, practices and procedures of the company to filling orders and making refunds promptly. Respondents concede that there are bound to be some mistakes which is part of the nature of the mail-order business (Resp. PF p. 21), but contend that Norris did not have such an unusual complaint record (Resp. PF p. 19) that would warrant a finding that they violated the provisions of the Federal Trade Commission Act.

In my opinion, it is respondents' regular business policies, practices and procedures that engender the basic "unfairness" in certain practices found in this matter. Respondents candidly admit that they cannot trace their shipments and accordingly cannot ascertain whether delivery of merchandise has been made. In response to complaints or inquiries about delivery they regularly make the assumption that the merchandise has been shipped and will be delivered soon. They do not check their records to see if shipment was actually made. They do not follow up to see if delivery was in fact subsequently accomplished. They assume that if nothing further is heard from the consumer, delivery was accomplished.

With respect to refunds, respondents take the position that if they received the returned merchandise, a refund was made, and conversely, if they did not send a refund, they did not receive the returned merchandise. They apparently make no automatic refunds on complaints that merchandise was not delivered, but eventually make a reshipment or refund after subsequent complaints are received.

The inherent unfairness in these procedures is that although the prospective customer is promised in respondents' advertisements that (1) they order at "no risk," (2) that delivery is "guaranteed" and (3) that the customer must be satisfied or his money will be refunded, respondents do not take the initiative in living up to these promises. If something goes amiss, the customer may be placed in a position where he must "hassle" respondents for the merchandise or the refund. In the circumstances, the incidents of complaints, [62] although perhaps relatively few in number as compared to the orders handled, cannot be termed "inconsequential." If any customer is placed in a position where he must "fight" for delivery or a refund, it is no excuse for respondents to say that the problems are part of the nature of the mail-order business. The answer is, and the Federal Trade Commission is mandated, to put a stop to the unfair practices.

Weight to be given testimony by consumer agency witnesses

Respondents contend that the testimony of the consumer agency witnesses must be afforded no weight and disregarded because it was founded on rank hearsay and cannot be relied upon as to the validity of the complaints reported (see Resp. PF p. 18). This testimony was not received for the truth of the complaints themselves, but for the fact that Norris' practices, the ones challenged in this proceeding, had often come to the attention of the consumer agencies. This merely tends to establish that the problem was more consequential than as established by the number of consumer witnesses who testified.

Except for the fact that the New York Attorney General's Office and the "Metropolitan Better Business Bureau" had forwarded consumer's letters of complaint to the Federal Trade Commission, no reliance was given to the testimony of Ms. Susan Metzger, Consumer Protection Specialist, Federal Trade Commission. The charts that she prepared were at the direction of complaint counsel for purposes of determining what possible allegations were to be included in a complaint, at that time still to be drafted. As demonstrated during cross-examination, it was difficult if not impossible for her to decipher the specifics of the consumer's complaint from the information on the charts. The degree of reliability of these exhibits was not such as to justify inclusion of them as evidence of record in this proceeding (see ALJ 1601-2).

About violations of the Federal Trade Commission Act

It is well settled that any advertising representation that has the tendency and capacity to mislead or deceive a prospective purchaser is an unfair and deceptive act and practice which violates the Federal Trade Commission Act. *Chrysler Corp.* v. *Federal Trade Commission,* D.C. Cir. No. 76-1586, *decided* July 6, 1977 at slip op. 12; *Charles of the Ritz Dist. Corp.* v. *Federal Trade Commission,* 143 F.2d 676, 679-80 (2d Cir. 1944). **[63]**

It is also a violation of the Federal Trade Commission Act to fail to disclose facts relevant to the advertising representation that, if known to the prospective purchaser, might affect his decision as to whether to purchase the advertised product. *Colgate-Palmolive Co., supra.*

The Federal Trade Commission may determine that certain practices are "unfair" when a seller does not live up to certain representations as to his performance in filling orders. See *Federal Trade Commission* v. *Sperry & Hutchinson* 405 U.S. 233 (1972). It is an unfair trade practice to retain moneys of consumers where performance on the transaction is not accomplished. *Windsor Distributing Co.,* 77 F.T.C. 204, *aff'd, Windsor Distributing Co.* v. *Federal Trade Commission,* 437 F.2d 443 (3d Cir. 1971).

In addition to the above type of "unfair" practices, complaint counsel contend that it is "unfair" for respondents not to maintain a telephone listing in a local telephone directory. They argue that consumers should be able to reach respondents by telephone in order to make complaints as to delivery or refunds.

I am not aware of any prior case, adjudicative or non-adjudicative, wherein respondent was held to have engaged in an unfair practice by *not* maintaining a public listing of its telephone or was ordered to maintain a public listing of its telephone number. Although it appears that the Commission's staff was concerned about this problem when it drafted the statement of basis and purpose of the Proposed Trade Regulation Rule on Mail Order Merchandising, the promulgated Rule does not contain any such requirement.

The Commission's promulgation of the Rule does not control this adjudicative proceeding, wherein determinations as to illegal conduct and appropriate remedies are made on the adjudicative record.

It certainly would be unfair for a seller to isolate himself from the consumer after the consumer has ordered and paid for a product and where the seller has guaranteed certain performance on the seller's part. But I do not think it is unfair merely to maintain an unlisted telephone, where other means of communication are available. Considering **[64]** the testimony of Mr. Fenvessey, as well as respondents' candid description of their procedures in processing orders and complaints, it would not appear very useful to *require* a general listing of their telephone number. The confusion and frustration that a great number of telephone inquiries would engender, if not processed properly, is not hard to imagine.

Coupled with the "telephone" issue, is the question of what type of response respondents should make to inquiries or complaints relating to delivery or refunds. In this respect, another question is what records respondents should maintain in order to upgrade their procedures for handling complaints and request for refunds. As pointed out above (see findings 22, 26; disc. p. 61), respondents, although they maintain computer information, do not use it to ascertain the status of the transaction that is subject to complaint or inquiry. The Trade Regulation Rule does require specific record keeping that would disclose such facts as well as respondents' actions on the complaints and inquiries. It may be that respondents, without much difficulty, could alter their computer capability to provide the information retrieval necessary for compliance with such requirements. There is no doubt that they must do something if they continue to make the representations that engendered the complaint in this matter.

Respondents contend that their practice of having customers document their purchase before respondents will process their claim for refund or reshipment is not unfair, in that most retail stores require presentation of the sales slips before making refunds on goods returned. But a retail store which provides a sales slip and a face-to-face confrontation between the customer and the seller, is in a different situation than a mail-order business that sells merchandise unseen, prepaid, by mail. As long as respondents represent that the customer will get a refund or that delivery is guaranteed, they cannot require the return of cancelled checks or other such proof of payment, as a condition for their acting on a complaint, unless they disclose to the customer in the original contact that such proof will be required before reshipment or refund is made.

Thus, failure to keep adequate records of mail orders is an unfair trade practice and a mail-order business can be required to maintain such records. In the circumstances of this case, failure to maintain a telephone listing is not by itself an unfair practice. [65]

The "telephone" issue has one more dimension. Once a customer does complain about nondelivery or failure of refund, it is an unfair practice not to provide them with a telephone number for future contacts. I think that at some posture of the transaction, respondents should disclose their telephone number. This is taken up in the remedy section which follows (see p. 73).

CONCLUSIONS

1. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of respondents Norris, Pan-Am, Jacobs, Williams and Mann.

2. This proceeding is in the public interest. The Commission so determined upon the assumption of jurisdiction through the issuance of the complaint. *American Airlines, Inc.* v. *North American Airlines, Inc.*, 351 U.S. 79, 83 (1956). Nothing in the record or findings requires a different determination. See *Federal Trade Commission* v. *Klesner*, 280 U.S. 19 (1929).

3. The individual respondents formulated, directed and controlled the acts and practices of the corporate respondents of which they were officers, including the acts and practices found herein.

4. Respondents Norris, Jacobs and Williams engaged in the following acts and practices as alleged in the complaint. They misrepresented that —

a. merchandise paid for by a certified check is always shipped to purchasers immediately;

b. merchandise paid for by a non-certified check is always shipped to purchasers about two weeks after said check has been approved for payment at the purchaser's bank;

c. the full purchase price of the product plus all additional charges paid by the purchaser in connection with said purchase are refunded by respondents if the purchaser is dissatisfied for any reason;

d. a sum of money in the form of cash, check, money order or other negotiable currency is always refunded to purchasers if they are dissatisfied for any reason; [66]

e. pursuant to respondents' 30-day money back guarantee, purchasers will always receive a full refund if the merchandise is returned to respondents within 30 days from the date of the purchaser's receipt of said merchandise;

f. in a substantial number of cases, the non-delivery of the purchaser's order, is caused by the United States Postal Service;

g. exchanges or refunds are always expeditiously processed by respondents;

h. all parcels shipped to purchasers, except those items marked express collect, are insured against loss, damage or other casualty by respondents.

In addition, these three respondents misrepresented that—

a. the "JN INSTA-JET PROPANE FLAME GUN" is able to whip through the heaviest snow drifts and the thickest ice in seconds and is effective and efficient in clearing walks and driveways of ice and snow;

b. respondents' roach powder is safe to use;

c. respondents' roach powder gets rid of roaches once and for all;

d. respondents' roach powder creates a deadly chain reaction which eliminates and kills roaches and eggs;

e. the manufacturer has unconditionally guaranteed that respondents' roach powder prevents reinfestation when used as directed and left in place or it will refund money;

f. respondents' roach powder does not lose its capacity to kill under any conditions of use;

g. respondents' TV antenna will bring sharp and clear reception even in difficult areas;

h. the performance of respondents' TV antenna is superior to any rabbit ear antenna or outdoor antenna; [67]

i. respondents' TV antenna is an electronic miracle;

j. respondents' "FIVE YEAR FLASHLIGHT" carries an absolute 5-year guarantee;

k. respondents' Lincoln-Kennedy penny was minted by the United States Treasury Department;

l. respondents' Lincoln-Kennedy penny is a coin of historical and numismatic significance which is certain to grow in value;

m. the issuance of respondents' Lincoln-Kennedy penny was sanctioned by Section 331, Title 18, U.S. Code;

n. a free plaque containing historical coincidence between the lives of President Lincoln and President Kennedy is provided to purchasers with each coin order.

In addition, these three respondents have failed to disclose the following material facts in their advertising that —

a. initial purchase of respondents' flame gun does not include the propane cylinder mentioned in respondents' advertisements of its flame gun. The propane cylinder, which is an essential component of the flame gun, must be purchased at an additional cost;

b. respondents' roach powder is 50% boric acid and 50% inert ingredients;

c. respondents' roach powder is hazardous. The product may be harmful to human beings and pets. Special precautions should be taken in the use of this product;

d. respondents' flashlight has an on life of 10 to 20 hours;

e. the manufacturer's guarantee of respondents' flashlight is not absolute. The manufacturer guarantees that the light can be stored and remain usable for 5 years or operate for a total of ten hours whichever comes first. [68]

In addition, these three respondents engaged in the following acts and practices —

a. deposited purchasers' checks and money orders into their bank accounts within three days to one week from receipt of such checks and money orders and have failed to either ship the merchandise ordered or to refund money for one month to one year;

b. failed to answer letters of inquiry from consumers or have made inadequate responses which have thereby delayed or prevented purchasers, seeking deliveries of merchandise or refunds of their money, from obtaining same;

c. placing the burden of record keeping upon the purchasers who, upon seeking a refund, exchange, or delivery of the advertised merchandise ordered and paid for by them, have been required by respondents to provide copies of their cancelled checks, original order blanks or various correspondence received from respondents as well as the full details pertaining to the merchandise ordered such as the size, color, price, style number and the date the order was placed.

5. Respondents Norris, Jacobs, Williams, Pan-Am and Mann engaged in the following acts and practices as alleged in the complaint. They misrepresented that —

a. cars delivered to purchasers are in good mechanical and physical condition;

b. cars delivered to purchasers are in safe operating condition;

c. cars are checked by expert mechanics and necessary repairs are made prior to release for delivery;

d. cars delivered to purchasers are in sound condition and repair and render normal, adequate and satisfactory service; [69]

e. respondents' cars may be readily resold by the purchasers at a profit;

f. cars are regularly ordered and received in advance of their being offered for sale and are held in stock until purchaser orders are received;

g. respondents' cars have undergone thorough and complete servicing and inspection before being released and approved for delivery.

In addition, these five respondents have failed to disclose that —

a. respondents' cars are ex-New York City taxicabs;

b. interiors of motor vehicles have not been cleaned or reconditioned by respondents prior to their being offered for sale.

6. The aforesaid acts and practices of respondents have the tendency and capacity to mislead and deceive the public and constitute unfair methods of competition and unfair and deceptive

acts and practices in commerce or affecting commerce in violation of the Federal Trade Commission Act.

7. In all other respects the allegation of the complaint as to violation of the Federal Trade Commission Act have not been sustained by the evidence or as a matter of law.

REMEDY

The Commission is vested with broad discretion in determining the type of order necessary to insure discontinuance of the unlawful practices found. *Federal Trade Commission* v. *Colgate-Palmolive Co.,* 380 U.S. 374, 392 (1965). The Commission's discretion is limited only by the requirement that the remedy be reasonably related to the unlawful practices found. *Jacob Siegel Co.* v. *Federal Trade Commission,* 327 U.S. 608, 613 (1946); *Warner Lambert Co.* v. *Federal Trade Commission,* D.C. Cir. No. 76-1138 (decided August 2, 1977) (slip opinion at page 24); *Niresk Industries Inc.* v. *Federal Trade Commission,* 278 F.2d 337, 343 (7th Cir. 1960), *cert. denied,* 364 U.S. 883. [70] The Commission is not limited to prohibiting the illegal practices in the exact form in which they were found to have been employed in the past and may close all roads to the prohibited goal. *Federal Trade Commission* v. *Ruberoid Co.,* 343 U.S. 470, 473 (1952); *Federal Trade Commission* v. *National Lead Co.,* 352 U.S. 419 (1957).

Counsel supporting the complaint have proposed an order to cease and desist that is somewhat narrower than the proposed order that accompanied the complaint (CSC PF pp. 81-96). Respondents in their proposed findings, although objecting to any order on the grounds of failure of proof, have specifically challenged certain features of the originally proposed order (Resp. PF pp. 101-117; see Resp. Ans. Par. 16, items a-r).

In the following discussion the new order proposed by complaint counsel will be used as a frame of reference. However, because many changes are required to conform the order to the findings in this decision as well as the requirements of law, the proposed order that follows is substantially different in format and content.

Pan-Am and Mann were not found to have been engaged in the general business practices attributable to Norris, Jacobs and Williams and which were found to be in violation of the Federal Trade Commission Act. Accordingly, the preamble to the principal portion of the order to cease and desist (Part I) relating to such practices will not include Pan-Am and Mann. On the other hand, those paragraphs of the order relating to practices in the sale of used cars by mail order (Part II) will run to Norris, Jacobs, Williams, Pan-

Am and Mann. All the above respondents will be subject to the general requirements of Part III of this order.

Respondent Mann contends that nothing in any order issued should relate to his business as an officer of Future Motors. It does not appear that Future Motors is engaged in a mail-order business. With the order limited to "mail-order sales" Mr. Mann's compliance should not involve him in his other capacity, unless Future Motors enters the mail-order business. Of course, Mr. Mann's future involvement in any mail-order business must be subject to the limited requirements of the order as it relates to him. [71]

Some of the prohibitions of complaint counsel's proposed order create absolute requirements on respondents irrespective of any representation they might make in their advertisements in the future. Such subjects as refunds and affirmative disclosures on respondents' flashlights and roach powder fall into this category. The requirements as to what makes up the refund total, *i.e.*, everything tendered at the time of the order, is proper only where respondents make a general money back guarantee. If they state exactly what will be refunded, they should not be required to refund more. Requirements as to disclosure of the "on time" life of the flashlight should be required only if respondents represent in any way the life expectancy of a battery or power source. Requirements in advertising as to the hazards of roach powder should be required only if respondents represent in any way that the product is safe (Compare CXSC Proposed Order Pars. 1, 3, 11, 12, 13; I.D. Order Par. 1, 3, 12, 13, 15).

Respondents object to paragraphs 4, 5 and 6 of counsel's proposed order on the grounds that those paragraphs are almost exactly the requirements of the Commission's Trade Regulation Rule for Mail-Order Merchandising, and that they are already required to comply with those requirements. They contend that they should not be subjected also to possible enforcement sanctions of a cease and desist order.

The illegal practices in which respondents were found to have engaged support these order provisions. It is proper for the Commission to include them in an order. They are reasonably related to the practices and close all roads to the prohibited goal. In effect, using the exact language insures that, except for a different enforcement posture, all members of the industry are subject to the same requirements.

In my opinion the "reasonable basis" requirement of Par. 4 relating to the availability of merchandise advertised for sale is proper, and the requirement that respondent document this "reasonable basis" is not onerous.

Complaint counsel propose a paragraph that requires respondents to have a "reasonable basis" to support any advertising claim they may make for the safety, efficacy, performance, content or any characteristic of any product. Respondents claim that the Commission does not have the power to issue such a prohibition in that it would penalize them for statements which were in fact true, and that in any event such a requirement is so vague and burdensome that it cannot be justified in this case. [72]

There is no doubt that the Commission has the power to require an advertiser to have a reasonable basis at the time claims are made concerning the technical attributes of any product. See *Firestone Tire & Rubber Co.* v. *Federal Trade Commission*, 481 F.2d 246 (6th Cir. 1973); *Fedders Corp.* v. *Federal Trade Commission*, 529 F.2d 1398, 1400–1 (2d Cir. 1976). However, as a practical matter, those cases where the Commission has applied the so-called "reasonable basis" substantiation involved complicated scientific data. The proposed paragraph requires a mail-order business to have "competent scientific tests" or "competent objective material" as a reasonable basis for all advertising claims for *all products* that it offers for sale. While it is true that respondents were found to have made claims for some of their products which were found to be false and misleading, the "reasonable basis" requirement of the order is too broad. In my opinion that paragraph should be modified to limit "reasonable basis" documentation to possession of and reliance on "competent objective material". In other words, respondents must rely upon something objective before making any product claims. See *Fedders*, *supra*, 529 F.2d at 1403–4.

Complaint counsel also include a paragraph that would require respondents to disclose the actual shipper of the merchandise, when they are not the shipper. The record in this case does not establish that failure to make this disclosure is "unfair." Clearly the other paragraphs of the order should eliminate any problem purchasers might encounter where goods are not shipped by respondents. Respondents deal with customers, will be the subject of the customer's complaint, and will be responsible for delivery or refund. Paragraph 8 of the proposed order will be deleted.

Respondents point out that the Commission's challenge to their Lincoln-Kennedy penny advertising duplicates, in all major respects, the issues raised in the proceeding brought by the United States Postal Service against them before the issuance of the complaint in this matter. (Resp. PF at pp. 61–63; see Finding 47, *supra*). They argue that the Commission's entry of an order to cease and desist as to their Lincoln-Kennedy penny advertisements is improper and unnecessary.

There is nothing improper in the Commission's proceeding under Section 5 of the Federal Trade Commission Act in areas already covered by Postal Service orders. There are many basic and material differences in the laws administered by the two public agencies. See *Reilly* v. *Pinkus,* 338 U.S. 269, 277 (1949); *Damar Products, Inc.,* 59 F.T.C. 1263 (1961), *aff'd, Damar Products, Inc.* v. *Federal Trade Commission,* 309 F.2d 323 (3d Cir. 1962). [73]

Respondents also argue that certain challenged practices should not be the subject of adjudication because they will be the only mail-order company subject to specific regulation. These areas, argue respondents, must be the subject of Rule Making Procedures (Resp. PF pp. 12, 82, 106-7, 115). The Commission is not estopped from proceeding by way of adjudication because a matter may also be the proper subject of Rule Making. Such a decision is for the Commission as a matter of policy. Insofar as respondents may be disadvantaged competitively from the strictures of an order to cease and desist, those caught violating the Federal Trade Commission Act must expect some fencing in. It should be pointed out, however, that the Commission, under the amendments contained in the Federal Trade Commission Improvement Act, may extend some proscriptions of the order issued against respondents to other mail-order businesses. See 15 U.S.C. 45(m)(1)(B).

In my opinion, complaint counsel's proposed order does not adequately cover the substantive unfair and deceptive advertising practices in which respondents were found to be engaged in connection with the offering for sale, sale and distribution of their FLAME GUN, LINCOLN-KENNEDY PENNY, TV ANTENNA, ROACH POWDER, and used automobiles. Paragraphs have been added which prohibit these specific practices.

Complaint counsel's proposed order does not prohibit misrepresentations that the consumer will receive something "free" in connection with the purchase of a product. A paragraph will be added covering this practice.

Respondents have been found to have misrepresented that they insure the shipments to customers. Complaint counsel recommend dropping the paragraph in the notice order (Par. 8) which relates to this practice. It will be retained in part.

The record-keeping requirements of the order are proper and the record in this case clearly demonstrates the need for such requirements.

As found above, respondents did not violate the Federal Trade Commission Act by using different corporate names, and in my opinion they are not required to "list" their telephone number in a local telephone directory. However in all correspondence relating to complaints they should disclose their telephone number, if, in fact, they do have a telephone. The order will be modified accordingly.

Finally, there is nothing improper or burdensome about the 30-day prior notice requirement as to any proposed change in the status of any respondent. [74]

ORDER

I

It is ordered, That Jay Norris Corp., a corporation, its successors and assigns, and Joel Jacobs and Mortimer Williams individually and as officers of said corporation, and respondents' officers, agents, representatives and employees directly or through any corporation, subsidiary, division, trade style, or other device, in connection with the advertising, offering for sale, sale and distribution of general mail-order merchandise in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

1. Failing to refund the amount required by paragraph 3, *infra*, in connection with the purchase of respondents' merchandise within the time specified in respondents' advertisements. If no time is specified, such refund must be made promptly.

2. Failing to disclose clearly and conspicuously in all advertisements or other promotional material, any charges to be paid by the purchaser for postage, insurance or for any other purpose in connection with the shipment or the return of merchandise. [75]

3. Failing to refund the full purchase price, of merchandise including postage, insurance, handling, shipping, or any other fee or charge paid by the purchaser any time refund is made to purchaser, unless respondents clearly state in their advertisement the exact nature of the refund including any items of the purchaser's expense that will not be refunded.

4. (A) Soliciting any order for the sale of merchandise to be ordered by the buyer through the mail unless, at the time of the solicitation, respondents have a reasonable basis to expect that they will be able to ship any ordered merchandise to the buyer: (1) within the time clearly and conspicuously stated in any such solicitation, or (2) if no time is clearly and conspicuously stated, within thirty (30) days after receipt of a properly completed order from the buyer; and

(B) Providing any buyer with any revised shipping date, as provided in paragraph 5 of this order unless, at the time any such revised shipping date is provided, respondents have a reasonable basis for making such representation regarding a definite revised shipping date; or [76]

(C) Informing any buyer that they are unable to make any representation regarding the length of any delay unless (1) respondents have a reasonable basis for so informing the buyer and (2) respondents inform the buyer of the reason or reasons for the delay.

A reasonable basis, for the purpose of this section, shall consist of records or other documentary proof establishing the use of systems and procedures which assure the shipment of merchandise in the ordinary course of business within any applicable time set forth in this order.

5. (A) Where respondents are unable to ship merchandise within the applicable time set forth in paragraph 4(A) above, failing to offer to the buyer, clearly and conspicuously and without prior demand, an option either to consent to a delay in shipping or to cancel his order and receive a prompt refund. Said offer shall be made within a reasonable time after respondents first become aware of their inability to ship within the applicable time set forth in paragraph 4(A), but in no event later than said applicable time.

(1) Any offer to the buyer of such an option shall fully inform the buyer regarding his right to cancel the order and to obtain [77] a prompt refund and shall provide a definite revised shipping date, but where respondents lack a reasonable basis for providing a definite revised shipping date the notice shall inform the buyer that respondents are unable to make any representation regarding the length of the delay.

(2) Where respondents have provided a definite revised shipping date which is thirty (30) days or less later than the applicable time set forth in paragraph 4(A), the offer of said option shall expressly inform the buyer that, unless respondents receive, prior to shipment and prior to expiration of the definite revised shipping date, a response from the buyer rejecting the delay and cancelling the order, the buyer will be deemed to have consented to a delayed shipment on or before the definite revised shipping date.

(3) Where the respondents have provided a definite revised shipping date which is more than thirty (30) days later than the applicable time set forth in paragraph 4(A), or where the respondents are unable to provide [78] a definite revised shipping date and therefore inform the buyer that they are unable to make any representation regarding the length of the delay, the offer of said

option shall also expressly inform the buyer that his order will automatically be deemed to have been cancelled unless (a) respondents have shipped the merchandise within thirty (30) days of the applicable time set forth in paragraph 4(A) above, and have received no cancellation prior to such shipment, or (b) respondents have received from the buyer within thirty (30) days of said applicable time, a response specifically consenting to said shipping delay. Where the respondents inform the buyer that they are unable to make any representation regarding the length of the delay, the buyer shall be expressly informed that, should he consent to an indefinite delay, he will have a continuing right to cancel his order at any time after the applicable time set forth in paragraph 4(A) by so notifying respondents prior to actual shipment.

(4) Nothing in this paragraph shall prohibit respondents when they furnish a definite revised shipping date to paragraph 5(A)(1) above, [79] from requesting, simultaneously with or at any time subsequent to the offer of an option pursuant to paragraph 5(A), the buyer's express consent to a further unanticipated delay beyond the definite revised shipping date. *Provided, however,* that where respondents solicit consent to an unanticipated indefinite delay the solicitation shall expressly inform the buyer that, should he so consent to an indefinite delay, he shall have a continuing right to cancel his order at any time after the definite revised shipping date by so notifying respondents prior to actual shipment.

(B) Where respondents are unable to ship merchandise on or before the definite revised shipping date provided under paragraph 5(A)(1), and consented to by the buyer pursuant to paragraphs 5(A)(2) and 5(A)(3), failing to offer to the buyer, clearly and conspicuously and without prior demand, a renewed option either to consent to a further delay or to cancel the order and to receive a prompt refund. Said offer shall be made within a reasonable time after respondents first become aware of their inability to ship before the said definite revised date, but in no event later than the expiration of the definite revised shipping date. *Provided, however,* [80] that where respondents previously have obtained the buyer's express consent to an unanticipated delay until a specific date beyond the definite shipping date, pursuant to paragraph 5(A)(4) or to a further delay until a specific date beyond the definite revised shipping date pursuant to paragraph 5(B), that date to which the buyer has expressly consented shall supersede the definite revised shipping date for purposes of paragraph 5(B).

(1) Any offer to the buyer of said renewed option shall provide the buyer with a new definite revised shipping date, but where

respondents lack a reasonable basis for providing a new definite revised shipping date, the notice shall inform the buyer that respondents are unable to make any representation regarding the length of the further delay.

(2) The offer of a renewed option shall expressly inform the buyer that, unless respondents receive, prior to the expiration of the old definite revised shipping date or any date superseding the old definite revised shipping date, notification from the buyer [81] specifically consenting to the further delay, the buyer will be deemed to have rejected any further delay, and to have cancelled the order if respondents are in fact unable to ship prior to the expiration of the old definite revised shipping date or any date superseding the old definite revised shipping date. *Provided, however,* that where respondents offer the buyer the option to consent to an indefinite delay the offer shall expressly inform the buyer that, should he so consent to an indefinite delay, he shall have a continuing right to cancel his order at any time after the old definite revised shipping date or any date superseding the old definite revised shipping date.

(3) Paragraph 5(B) shall not apply to any situation where respondents, pursuant to the provisions of paragraph 5(A)(4), have previously obtained consent from the buyer to an indefinite extension beyond the first revised shipping date. [82]

(C) Whenever a buyer has the right to exercise any option under this order or to cancel an order by so notifying respondents prior to shipment, failing to furnish the buyer with adequate means, at respondents' expense, to exercise such option or to notify respondents regarding cancellation. For the purpose of this order, "adequate means" requires respondents to:

(1) Provide any offer, notice or action required by this order in writing and by first class mail;

(2) Provide the buyer with the means in writing (by business reply mail or with postage prepaid by respondent) to exercise any option or to notify respondents regarding a decision to cancel.

Nothing in paragraph 5 of this order shall prevent respondents where they are unable to make shipment within the time set forth in paragraph 4(A) or within a delay period consented to by the buyer, from deciding to consider the order cancelled and providing the buyer with notice of said decision within a reasonable time after they become aware of said inability to ship, together with a prompt refund. [83]

6. Failing to deem an order cancelled and to make a prompt refund to the buyer whenever:

(A) Respondents receive, prior to the time of shipment, notification from the buyer cancelling the order pursuant to any option, renewed option or continuing option under this order;

(B) Respondents have pursuant to paragraph 5(A)(3), provided the buyer with a definite revised shipping date which is more than thirty (30) days later than the applicable time set forth in paragraph 4 (A) or have notified the buyer that respondents are unable to make any representation regarding the length of the delay and respondents (1) have not shipped the merchandise within thirty (30) days of the applicable time set forth in paragraph 4(A), and (2) have not received the buyer's express consent to said shipping delay within said thirty (30) days.

(C) Respondents are unable to ship within the applicable time set forth in paragraph 5(B) and have not received, within the said applicable time, the buyer's consent to any further delay;

(D) Respondents have notified the buyer of their inability to make shipment and have indicated their decision not to ship the merchandise; or [84]

(E) Respondents fail to offer the option prescribed in paragraph 5(A) and have not shipped the merchandise within the applicable time set forth in paragraph 4(A).

For purposes of this order:

(1) "Shipment" shall mean the act by which the merchandise is physically placed in the possession of the carrier.

(2) "Receipt of a properly completed order" shall mean the time at which respondents receive an order from the buyer containing all the information requested by respondents and accompanied, where required, by the proper amount of money in the form of cash, check or money order. *Provided, however,* that where respondents receive notice that the check or money order tendered by the buyer has been dishonored or that the buyer does not qualify for a credit sale, "receipt of a properly completed order" shall mean the time at which (a) respondents receive notice that a check or money order for the proper amount tendered by the buyer has been honored, (b) the buyer tenders cash in the proper amount or (c) the seller receives notice that the buyer qualifies for a credit sale.

(3) "Refund" shall mean:

(a) Where the buyer tendered full payment for the unshipped merchandise in the form of cash, check or money order, a return of *the full amount* tendered in the form of cash, check, or money order;

(b) Where there is a credit sale:

(i) and the seller is a creditor, a copy of a credit memorandum of the like or an account statement reflecting the removal or absence of any remaining charge incurred as a result of the sale from the buyer's account;

(ii) and a third party is the creditor, a copy of an appropriate credit memorandum or the like to the third party creditor which will remove the charge from the buyer's account or a statement from the seller acknowledging the cancellation of the order and representing that he has not taken any action regarding the order which will result in a charge to the buyer's account with the third party;

(iii) and the buyer tendered partial payment for the unshipped merchandise in the form of cash, check or money order, a return [86] of the amount tendered in the form of cash, check or money order.

(4) "Prompt refund" shall mean:

(a) Where a refund is made pursuant to definition (3)(a) or (3)(b)(iii) a refund sent to the buyer by first class mail within seven (7) working days of the date on which the buyer's right to a refund vests under the provisions of this order.

(5) The "time of solicitation" of an order shall mean that time when respondents have:

(a) Mailed or otherwise disseminated solicitation to a prospective purchaser;

(b) Made arrangements for an advertisement containing the solicitation to appear in a newspaper, magazine or the like or on radio or television which cannot be changed or cancelled without incurring substantial expense, or

(c) Made arrangements for the printing of a catalog, brochure or the like which cannot be changed without incurring substantial expense, in which the solicitation in question forms an insubstantial part.

7. Representing the safety, efficacy, performance, content or any other characteristic of any product unless [87] such claims are fully and completely substantiated by a reasonable basis which shall consist of competent objective material and such substantiative material is available to the public.

8. Misrepresenting that the nondelivery of merchandise ordered and paid for by a customer is caused by loss of the merchandise by the United States Postal Service.

9. Misrepresenting, directly or indirectly, the time or manner in which respondents' flame gun, or any other product used for the removal of snow or ice, will perform in the removal of snow or ice.

10. Failing to disclose, clearly and conspicuously, in all advertisements or other promotional material that the purchase price of respondents' flame gun or any other product does not include all components necessary for its operation and failing to identify the

component(s) which are not included in the purchase price, if such is the fact.

11. Misrepresenting, directly or indirectly, the time in which or the manner by which respondents' roach powder, or any other pesticide product, will kill or eliminate roaches.

12. Making any representation as to the safety of respondent's roach powder or any other pesticide [88] product without failing to disclose, clearly and conspicuously, in all advertisements or other promotional material for said products, the exact ingredients and percentage(s) of such ingredients contained therein.

13. Making any representation as to the safety of respondents' roach powder or other pesticide product without failing to clearly and conspicuously include the following statement in all advertisements and other promotional material for said products: "This product may be hazardous to your health and the environment. Read the label and use only as directed."

14. Misrepresenting, directly or indirectly, that respondents' TV antenna or any TV antenna will bring in sharp and clear reception and is superior to any other antenna.

15. Making any representation as to the life expectancy of flashlights or other similar battery operated product without failing to disclose, clearly and conspicuously in all advertisements and other promotional material for such products (a) the expected "on" life of the product; and (b) any limitations on the warranty of such product. [89]

16. Representing, directly or indirectly, that the Lincoln-Kennedy penny was minted by the United States Treasury Department.

17. Representing, directly or indirectly, that the Lincoln-Kennedy penny is a coin of historical and numismatic significance which is certain to grow in value.

18. Representing, directly or indirectly, in connection with the sale of any product that another product is given "free" or as a gift or without cost or charge in connection with:

a. any offer which runs for an indefinite term or continuously for a period in excess of one (1) year;

b. any offer not covered by (a) above, excluding introductory offers, unless as to such limited offer:

(1) a regular bona fide retail price is established for the product without the "free" product;

(2) a regular bona fide retail price is established for the "free" product, or in the absence of such price a determination is made of the cost to respondents of such other product; and [90]

c. the price of the product is reduced at least as much as the price or cost of the "free" product.

19. Failing to include the name "Jay Norris" or "Jay Norris Corporation" and an address and telephone number to which consumer complaints may be addressed in all correspondence relating to customer complaints.

20. Failing to maintain records of all orders, payments and shipments made by or received by respondents, including, but not limited to the following information:

a. Name and address of the customer;
b. Color, size, quantity, price, style number of merchandise ordered;
c. Date of receipt of the order;
d. The form of payment (check, cash, money order, credit sale);
e. Date and method of shipment of merchandise, including whether or not the shipment was insured and the amount of insurance, if any;
f. Date and form of refund, if any, and reason for such refund.

21. Failing to maintain records of all consumer complaints for a period of three years after such complaint is received, including, but not limited [91] to the following information:

a. Name and address of the consumer;
b. Date of receipt of the complaint;
c. Transaction about which complaint is received;
d. Nature of the complaint;
e. Date and disposition of the complaint.

II

It is further ordered, That Jay Norris Corp., and Pan-Am Car Distributors Corp., corporations, their successors and assigns, and Joel Jacobs, Mortimer Williams and Kenneth Mann, individually and as officers of said corporations, and respondents' officers, agents, representatives and employees directly or through any corporation, subsidiary, division, trade style, or other device, in connection with the advertising, offering for sale, sale and distribution of used automobiles by mail-order in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

1. Failing to disclose, clearly and conspicuously in all advertisements, correspondence, or other promotional material for automobiles that:

(a) Interiors of motor vehicles have not been cleaned or reconditioned by respondents prior to their being offered for sale, if such is the fact. [92]

(b) The used motor vehicles offered for sale by the respondents are ex-New York City taxicabs, if such is the fact.

2. Representing, directly or by implication, the ease or profit with which purchasers can resell respondents' automobiles.

3. Shipping, or causing to be shipped, any automobile which does not comply with all motor vehicle registration, safety and inspection standards of the state within which the automobile is being shipped or sold.

4. Misrepresenting the mechanical and physical condition of said automobiles;

5. Misrepresenting that said automobiles are in safe mechanical and operating condition;

6. Misrepresenting the extent to which said automobiles have been inspected and repaired in preparation for sale and delivery to customers; and

7. Misrepresenting that said automobiles are in sound condition and repair and will render normal, adequate and satisfactory service.

III

It is further ordered, That:

1. Respondents shall notify the Commission at least thirty (30) days prior to any proposed changes [93] in the corporate respondents such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other changes in the corporation which may affect compliance obligations arising out of the order.

2. The individual respondents named herein, shall promptly notify the Commission of the discontinuance of their present business or employment and of their affiliation with a new business or employment. Such notice shall include respondents' current business address and a statement as to the nature of the business or employment in which they are engaged as well as a description of their duties and responsibilities.

3. Respondents shall deliver a copy of this order to cease and desist to all personnel or agents of respondents responsible for the preparation, creation, production or publication of the advertising of all products covered by this order.

4. No provision of this order shall be construed in any way to annul, invalidate, repeal, terminate, modify or exempt respondents from complying [94] with agreements, orders or directives of any

kind obtained by any other agency or act as a defense to actions instituted by municipal or state regulatory agencies. No provision of this order shall be construed to imply that any past or future conduct of respondents complies with the rules and regulations of, or the statutes administered by the Federal Trade Commission.

IV

It is further ordered, That the allegations of the complaint are dismissed as to FEDERATED NATIONWIDE WHOLESALERS SERVICE, GARYDEAN CORP., t/a Nationwide Wholesalers Service, and P-N PUBLISHING COMPANY, INC.

OPINION OF THE COMMISSION

By CLANTON, *Commissioner*:

This proceeding challenges the lawfulness of a variety of claims made in connection with the advertising of mail [2] order products. Respondents, since 1953, have advertised and sold through the mails a wide range of generally low-cost consumer products.[1] [3]

The complaint alleges, and the administrative law judge ("ALJ") found, that respondents, among other things, failed to live up to advertised promises of immediate delivery and prompt refunds and misrepresented the performance or characteristics of six specific products. In their appeal from the ALJ's initial decision, respondents not only attack the factual and legal bases of the proposed findings but also vigorously challenge the breadth and stringency of the recommended order.[2] Our consideration of these issues follows:

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[1] The respondents in this proceeding are Jay Norris, Inc.; Joel Jacobs and Mortimer Williams, who are the sole shareholders, officers and directors of Norris (ID 2); Pan Am, which was in the business of advertising and selling cars to consumers by mail (ID 5, 12); and Kenneth Mann, who together with Jacobs and Williams are the shareholders, officers and directors of Pan Am (ID 3). The ALJ dismissed the complaint as to Federated Nationwide Wholesalers Service, Garydean Corp., t/a Nationwide Wholesaler Service, and P-N Publishing Company, Inc. (ID p. 58). The term "respondents" hereinafter refers to the Jay Norris Corp., Joel Jacobs, and Mortimer Williams (and includes Pan Am and Kenneth Mann only as to ex-taxis). The following abbreviations are used in this opinion:

ID — Initial Decision, Finding No.
ID p. — Initial Decision, Page No.
CX — Complaint Counsel Exhibit No.
RX — Respondents' Exhibit No.
Tr. — Transcript of Testimony, Page No.
RAB — Respondents' Appeal Brief, Page No.
CAB — Complaint Counsel's Answering Brief, Page No.
RRB — Respondents' Reply Brief, Page No.
CPF — Complaint Counsel's Proposed Finding, Page No.
RPF — Respondents' Proposed Finding, Page No.
TROA — Transcript of Oral Argument, Page No.

[2] Respondents do not appeal from the ALJ's finding that the individual respondents Jacobs and Williams are properly held responsible for wrongdoing by the corporate respondent Jay Norris. Similarly, complaint counsel have not contested any of the allegations dismissed by the law judge.

I. *Immediate Delivery and Prompt Refund Claims*

The record quite clearly discloses that respondents made frequent statements in their catalogs and advertisements emphasizing the timeliness with which they effect delivery and issue refunds. These include representations such as "prompt delivery guaranteed," (CX 4) "immediate delivery guaranteed," (CX 8) or "to insure immediate delivery . . . please have check certified." (CX 409) For non-certified checks, respondents asked customers to "allow about 2 weeks until your check clears the bank." (*Id.*) Similar claims, of "prompt refund(s)" were made in connection with respondents' promises of money back guarantees for unsatisfied purchasers. (ID 17)

These and other representations were found to be deceptive by the law judge who noted, for example, that with respect to respondents' delivery claims they have "on numerous occasions deposited customers' checks or cashed money orders, and have not shipped the ordered merchandise for many months after receipt of the order and payment." (ID 24) The ALJ also found that many purchasers had encountered long delays in getting refunds and in some instances no refund was ever received. (ID 29, 32) [4]

Respondents do not deny making claims of "immediate delivery" or "prompt refunds," or even failing to fulfill such promises on occasion. Rather, they assert that the key issue is what consumers are reasonably entitled to expect in terms of the reliability of those promises. Every performance claim whether it be fuel economy in a car, durability in a toaster, or prompt service by a mail order company, expressly or impliedly represents how often that level of performance can be expected. Here, though their promises are unqualified, respondents nevertheless contend that the failure to make prompt deliveries and refunds 100 percent of the time does not necessarily compel the conclusion that their claims are false. Indeed, respondents argue that the magnitude of untimely deliveries and refunds—compared to their total sales—is relatively insignificant. To recharacterize this issue, when consumers read respondents' advertisements do they believe the statements implicitly represent, for example, that "all," "nearly all" or "most" purchasers would receive prompt delivery and refunds?

The record contains little direct evidence as to what degree of reliability the consuming public expected when it read these ads.[3] It is well established, however, that the Commission may determine the meaning of an ad without the aid of consumer testimony as to how the advertisement is perceived by the public. *E.g., Chrysler Corp.* v. *FTC*, 561 F.2d 357, 363 (D.C. Cir. 1977). Nor can it be doubted "that where an advertisement conveys more than one meaning, one of which is false, the advertiser is liable for the misleading variation. . . ." *National Commission on Egg Nutrition*, 88 F.T.C. 89, 186 (1976), *enforced in part*, 570 F.2d 157 (7th Cir. 1977), *petition for cert. filed*, 46 USLW 3694 (April 28, 1978). [5]

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[3] In examining this issue, it is useful to note that a principal factor underlying promulgation of the Mail Order Merchandise TRR, 16 C.F.R. 435 (1975), was the frequent failure of mail order companies to deliver ordered goods within a reasonable time. As we noted there, the regulation of delivery procedures was called for in view of evidence "that substantial numbers of consumers are not getting mail order merchandise shipped within that time which consumers had been led to believe shipment would be made." 40 F. R. 51582, 51587 (1975). Much the same question is involved here.

After examining respondents' ads in their overall context, we believe the evidence is clear that they represented that timely deliveries and refunds would be effected virtually without exception. Common sense suggests that a person reading an ad promising "immediate delivery" would be entitled to rely upon that claim with a fairly high degree of confidence that it would be fulfilled. Respondents' ads go even further. For example, their claims guaranteeing prompt delivery (CX 2, 4, 8) indicate to consumers that respondents take extraordinary precautions to insure speedy deliveries.[4] Similarly, respondents make unqualified claims of prompt refunds. (CX 386) Moreover, these refund claims are placed amidst claims of "your guarantee of satisfaction" (CX 57, 409), "no risk coupon" (CX 2, 4, 8) and "use . . . at our risk" (CX 96A-D, 886). Indeed, respondents' ads abound with claims that imply a purchaser cannot lose. We believe the rather unequivocal message conveyed by these ads is that respondents not only afforded their customers the opportunity to return any and all merchandise but also promised that such refunds would be made in a timely fashion in virtually every instance. Even if consumers might not expect absolute perfection, they could reasonably anticipate from reading respondents' ads that a far more reliable level of performance would be forthcoming than actually occurred. [6]

We find persuasive record support from which to conclude that respondents failed to make timely deliveries and refunds to numerous customers and that respondents' representations to the contrary were misleading and deceptive. The record is replete with testimony of consumers who experienced delivery or refund difficulties with respondents. (ID 18)[5] Abundant evidence also exists that many customers took the time to write their complaints to respondents, government agencies, consumer protection groups and magazines (ID pp. 9-15, 21-24).[6] These efforts are particularly noteworthy since most of the respondents' products are low price items for which many consumers are not likely to incur the trouble and expense of complaining. (CX 405-409) Thus, contrary to respondents' assertions, the testimony supplied by the 30 consumer witnesses, supplemented by the other evidence of consumer complaints, undoubtedly reflects the proverbial "tip of the iceberg."

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[4] Respondents argue that guaranteed should not be interpreted to represent greater reliability. Indeed, in another context they argue that "a money back guarantee carries with it a representation that the product might not effectively treat all cases" (RAB n. 37). In the case of deliveries this contention is clearly without merit. When delivery is late, respondents do not offer pecuniary compensation. The consumer is afforded no additional recourse. Given this context, if "guaranteed" is to have any meaning at all, it is that respondents' claim of prompt delivery is extremely reliable. *See* F.T.C. Guide Against Deceptive Advertising of Guarantees, 16 C.F.R. 239.7; *All State Industries of North Carolina, Inc.*, 75 F.T.C. 465, 488–89 (1969), *aff'd*, 423 F.2d 423 (4th Cir.), *cert. denied*, 400 U.S. 828 (1970).

Moreover, we agree with the ALJ that the procedures employed by respondents for recording, tracking, and responding to orders, complaints, and requests for refunds provide little solace to respondents in attempting to demonstrate the veracity of their claims. As the law judge observed: [7]

> . . . Respondents candidly admit that they cannot trace their shipments and accordingly cannot ascertain whether delivery of merchandise has been made. In response to complaints or inquiries about delivery they regularly make the assumption that the merchandise has been shipped and will be delivered soon. They do not check their records to see if shipment was actually made. They do not follow up to see if delivery was in fact subsequently accomplished. They assume that if nothing further is heard from the consumer, delivery was accomplished.
>
> With respect to refunds, respondents take the position that if they received the returned merchandise, a refund was made, and conversely, if they did not send a refund, they did not receive the returned merchandise. They apparently make no automatic refunds on complaints that merchandise was not delivered, but eventually make a reshipment or refund after subsequent complaints are received. (ID p. 61)

Notwithstanding these meager recordkeeping efforts and their demonstrated effect on delays in delivery and refunds, respondents contend that their performance relative to total sales is good.[7] The basis of this claim is respondents' colorfully described but rather simplistic "bucket method" of measuring complaints. Mr. Jacobs described this method when he explained how respondents calculated the ratio of complaints to sales: [8]

> A. I can tell you this. They [complaints] are going down percentage-wise because we measure by buckets. It's unusual. But our mail arrives and is kept in buckets. And we know that whereas years back we used to get "X" amount of buckets on a Monday and

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[5] Although respondents question the probity of some of this testimony (RAB at 16-17), our review of the record convinces us of its reliability. (*See also* CAB at 11-13)

[6] As the ALJ correctly noted, this testimony by so-called "consumer experts" need not be discounted as being hearsay, since it was received not for the truth of the complaints, but rather to show that consumer dissatisfaction extended beyond the consumer witnesses who testified.

[7] Similarly, respondents claim their performance compared with competing mail order companies is good (RAB at 20-22; RPF at 22-25). These comparisons to the performance of other mail order companies are largely irrelevant. The issue here is whether respondents' practices render their claims of prompt performance deceptive. Consequently, we are concerned with what consumers expect and whether respondents met those expectations.

> "X" amount on any other given day, that with each succeeding year, the number of buckets coming in each year is less.
>
> As far as the amount is concerned, percentage-wise again, I would estimate that it probably is running now about 2% . . . of orders received. . . (Tr. 147)

This measuring rod is far too susceptible to error for us to place much confidence in these figures.[8] Clearly it does not indicate that respondents' failure to back up their claims was a rare occurrence. To the contrary, the evidence suggests that respondents had no basis for making the sweeping claims about delivery and refunds set forth in their advertisements.

Thus, in view of the record, respondents' representations of immediate delivery and prompt refunds were false and deceptive. [9]

II. *Miscellaneous Delivery and Refund Claims*

Respondents also made a variety of other delivery and refund claims in their advertising which the ALJ found to be deceptive. These ads represented that (1) the full purchase price, plus all additional charges, would be refunded to dissatisfied purchasers (ID 15, 16); (2) refunds would be made in negotiable currency (ID 15, 16); (3) nondelivery was frequently the fault in the Postal Service (ID 22); and (4) all shipments were insured against loss or damage (ID 15).[9] We agree with the ALJ's determinations concerning each of the first three claims but disagree as to the fourth.

Respondents boldly make claims of "no risk" and "full refund" but candidly concede that they normally did not return the full amount tendered in payment by consumers (RAB at 52). Though some consumers may not have expected to be reimbursed for postage and handling charges *(Id.),* other consumers took a different view and demanded and received a refund for these additional charges (ID 27). In the face of express statements that purchasers incur "no risk," there is little doubt in our view that many, if not most, consumers would expect a full refund of the amount tendered. Similarly, in connection with the second claim, respondents also admit that for small amounts and under other circumstances they did not send the refund in a negotiable currency (ID 28). No such limitation can be read into respondents' advertising and in the absence of qualifying language we suspect that consumers would normally anticipate payment of a promised refund to be in the form of cash or its equivalent. [10]

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[8] Apart from this testimony, nowhere in the record do we find systematic evidence of respondents' overall delivery and refund performance. Absent these more revealing measures, we are not left impotent. Even rougher measures of consumer dissatisfaction when coupled with our previous experience with consumer complaints reveal the significant failings that plagued respondents' operations.

[9] A separate allegation that respondents misrepresented the extent to which they would absorb part of the delivery costs was dismissed by the ALJ for lack of evidence. (ID p. 31)

As for the third claim, respondents repeatedly represented that poor mail service was the cause of a delayed delivery or refund, rather than admitting that they were frequently to blame. (ID pp. 21, 22, 30) The prospect of losing customers to competitors is an important check on deceptive or just plain inefficient business practices. To avoid such competitive consequences, however, respondents attempt to mollify understandably upset customers by indiscriminately placing the blame on the U.S. Postal Service. Such efforts to hold onto consumers' business and induce repeat purchases are themselves deceptive.

Finally, we find respondents' claim that parcels shipped to purchasers are insured to be misleading. In reaching the same conclusion, the ALJ noted that:

> Respondents are self-insured; that is, instead of paying for public insurance on shipments, they make shipments at their own risk. Because they can not trace shipments, they make all necessary replacements at their own expense and at no charge to the customer (Jacobs 146–147; Williams 200). (ID 21)

Undoubtedly, most consumers would probably assume that reference to insurance means third-party insurance, and accord greater significance to the protective value of such insurance than to self-insurance. Nevertheless, respondents' use of the term "insurance" appears only in that part of their catalogs which sets out the additional charges for such items as handling and shipment. *See e.g.*, CX 407 p. 52. While technically deceptive, this brief mention of insurance at a point where most consumers would have already decided whether to purchase merchandise is not likely to have more than a *de minimis* effect. Given this situation and the limited frequency with which the reference appeared after Jay Norris stopped carrying insurance for its shipments, we see no need for an order provision addressing this issue. In any event, it is quite apparent that consumer dissatisfaction with respondents' delivery and refund practices stems from reliance upon overblown claims of timely service and full refunds rather than unfulfilled promises about insurance. [11]

III. *Performance Claims for Specific Products*

Apart from their more general mail order claims, the ALJ further determined that respondents deceptively advertised six specific products: (1) a propane flame gun, (2) a roach insecticide, (3) a flashlight, (4) a collector's coin, (5) a television antenna, and (6) ex-taxicabs.[10]

A. *J-N Insta-Jet Propane Flame Gun* The complaint alleged and the ALJ found that respondents represented that "THE J-N INSTA-JET PROPANE FLAME GUN" is able to whip through the heaviest snow drifts and the thickest ice in seconds and is effective and efficient in clearing walks and driveways of ice and snow."[11] (ID 43)

The record contains ample evidence of the flame gun's inefficacy in removing ice. A representative of a private testing firm, Mr. John Lomash, testified as to the length of time required for a propane flame gun to melt one square foot patch of ice at 0° fahrenheit. He found that the flame gun required 6.5 minutes to melt a patch 1/8 inch thick and 11 minutes to melt a patch 1/4 inch thick (ID 43; Tr. 1249–53). Mr. Lomash conceded that at warmer temperatures the ice would melt more quickly. (Tr. 1249–50) Respondents contend that because the record fails to reveal the typical conditions confronting an ordinary user, the test results do not prove that the flame gun is ineffective. Such an argument is misplaced, however, since respondents do not qualify their performance claims to limited temperature conditions. Indeed, respondents' broad representations suggest that the consumer will meet with success even in the worst weather: [12]

> Fastest Way We Know To Clear Away Ice and Snow
>
> . . . clears away ice and snow faster than you'd believe possible: Whips through even the heaviest drifts. Clears walks and driveways. . . (CX 2, 4)

It is not difficult to imagine that many of the consumers attracted to this alleged time-saving snow-removal product would hail from the northern reaches of the country where they would be all too likely to encounter Mr. Lomash's "test conditions" in real life.

Moreover, the experience of the three consumers who testified about the propane flame gun is equally persuasive evidence of the gun's inability to melt snow and ice quickly. (ID 43) Respondents challenge the credibility of this testimony because these consumers were unable to assure respondents' counsel that the flame guns they used were in operable condition. The record suggests, however, that the guns did produce flames (Tr. 342–343, 603, 1494) and were apparently being used for the first time (Tr. 342, 603–604, 1493–1494).

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[10] The ALJ dismissed another allegation that respondents misrepresented an allegedly long-wearing sock (ID 45).

[11] Respondents object to the reference to "in seconds" in the complaint. It seems this phrase was used only in connection with a kerosene flame gun. (ID 43) Nevertheless, we believe the ALJ correctly concluded that respondents' advertisements conveyed the impression that their product would rapidly remove snow and ice. For example, respondents claim that the flame gun will "whip through even the heaviest drifts" of snow and is "the fastest way [they know of] to clear away ice and snow." (ID 43)

Further, we note that the assembly process involves only three parts (Tr. 603) and is relatively uncomplicated. (Tr. 613) More importantly, we reject respondents' supposed rule that would virtually eliminate the utility of consumer testimony except in the rare case where a consumer could assure with certainty that the product used was functioning properly. While the credibility of such testimony is always a relevant issue, there is nothing here to suggest that it should be discounted. Indeed, we find the similar experience of these three consumers strong evidence that respondents' performance claims greatly exaggerate the flame gun's ability to melt snow and ice quickly.[12] [13]

B. *Sure Kill Roach Powder* Respondents sell a product composed of equal parts boric acid and inert ingredients whose purpose is the elimination of the ubiquitous household pest — the cockroach. In their advertising respondents represented, *inter alia*, that their roach powder:

. . . is safe to use;
. . . gets rid of roaches once and for all;
. . . creates a deadly chain reaction which eliminates roaches and eggs;
. . . is guaranteed to prevent reinfestation for up to 5 years; and
. . . does not lose its capacity to kill under any conditions of use. (ID 44)

In addition to finding that these claims were not supportable, the law judge also concluded that respondents failed to disclose a material fact by not specifying in their advertising the chemical ingredients of the insecticide. Respondents, not surprisingly, disagree with these findings.

(1) Safety. No one disputes that boric acid, a main component of respondents' roach powder, is toxic to warm blooded animals if taken internally (Tr. 1351-1352). At the same time, complaint counsel's primary witness, Dr. Charles Mampe, acknowledged "that respondents' roach powder is relatively safe to use if applied according to instructions" (CX 2493C). Because respondents' roach powder is one-half boric acid, however, it is virtually no less lethal than the less concentrated but more toxic chlorinated hydrocarbon insecticides (*compare* Tr. 1391; CX 2493C with CX 2493D). Indeed, roughly four tablespoons of this roach powder could kill a grown man (Tr. 1353; CX 2493D). Given such hazards, it is clearly deceptive to make an unqualified representation of safety for this product. Respondents cannot simply advertise as "safe" this noxious insecticide and hope mail order consumers will read the label and use the product as directed. [14]

(2) Efficacy. The record, particularly Dr. Mampe's testimony,

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[12] We also leave intact the ALJ's ruling, which respondents do not challenge, requiring disclosure that the flame gun does not come equipped initially with a propane cylinder.

amply supports the ALJ's findings that respondents misrepresented that this roach powder will kill roach eggs (Tr. 1366, 1380-1381) and will create a deadly chain reaction (Tr. 1356, 1424).[13] Respondents also claim their product will provide long-term, if not permanent, relief from cockroaches and will retain its effectiveness under varying conditions of use. While we are confident that few consumers would believe anything short of divine intervention could afford them eternal relief from this troublesome pest, respondents' ads are sufficiently specific (*e.g.*, Sure-Kill "never loses its killing power—even after years.") to impart a degree of believability to these claims that consumers might reasonably rely upon. A review of the testimony, including that given by the inventor and manufacturer of this product, Mr. Williams, thoroughly demonstrates the falsity of such claims. (Tr. 1357-1359; 1423) [15]

(3) Advertising Disclosure of Ingredients. Noting that boric acid is a well-known roach killer, the ALJ concluded that respondents' advertising should disclose the fact that their roach powder is 50 percent boric acid. We are not convinced, however, that this disclosure is of material benefit to consumers. The proposed disclosure, for example, provides consumers no basis for determining the importance of the other ingredients in respondents' product. Indeed, there is some suggestion that these inert ingredients significantly improve the effectiveness of the powder by making it more attractive to roaches. (RAB at 37) Complaint counsel counter by contending that respondents could inform consumers that these inert ingredients are significant. (TROA at 41) This argument misses the mark. If respondents' product significantly surpasses boric acid at killing roaches, it may be of little consequence to consumers that the powder is half boric acid.

Even if this information might be helpful to some consumers, that is not sufficient to render its nondisclosure deceptive. To the extent consumers have been misled by respondents' advertising into believing that the roach powder has special properties or capabilities, it is due to the exaggerated claims made in those ads. Requiring prior substantiation for future claims should serve as an adequate remedy to eliminate these misrepresentations. Without a stronger showing of materiality we see no justification for requiring disclosure of the ingredients in advertising. [16]

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[13] We are unimpressed with respondents' argument that a residue of the powder on roach eggs will kill the roaches when they hatch. (RAB at 36) The label directions instruct the consumer to place the powder in small trays (CX 3020, 4060) or to dust in cracks, crevices and building voids (CX 4186). The accumulation of powder on roach eggs could occur only if the dusting happened to reach eggs or if a contaminated roach returns to the next and transfers sufficient quantities of the powder to eggs and other roaches to start a "chain reaction." Mr. Williams, inventor of this roach powder, testified that he has personally observed contaminated cockroaches return to the nest and transfer the insecticide to eggs and other roaches (Tr. 1424). He conceded, however, that the chain reaction does not always occur and is not the primary way of killing roaches *(Id.)*. Moreover, Dr. Mampe seriously questioned whether the powder would be transferred to other roaches in sufficient amounts to kill them (Tr. 1393-1394). We find that respondents' claims both as to the destruction of eggs and the creation of a chain reaction are deceptive.

C. *Flashlight* In their advertising for this product, respondents refer to it as "The Five-Year Flashlight" and represent that it carries an "Absolute Five-Year Guarantee." (CX 46) In finding this advertising deceptive, the ALJ looked to the underlying manufacturer's guarantee which clearly states:

> Your light is also guaranteed to remain usable for a period of five years providing it has not been used for more than 10 hours. (CX 2044B)[14]

Neither this limitation nor the fact that the flashlight has an "on-life" of 10-20 hours were disclosed in respondents' advertisements. By not doing so, the ALJ determined that respondents failed to disclose material facts necessary to prevent the ads from being misleading. (ID 46) Respondents, while not disputing the terms of the guarantee, argue that the ads must be read in their total context. When the ads are so viewed, they contend, it is clear that the five-year claim refers to the storage capacity of the flashlight, not its on-time life.

There is no doubt that the ads emphasize the unique capability of the flashlight to retain its power over long periods of time. Nevertheless, we decline to graft, by implication, a normal use (*i.e.*, 10 hours) limitation onto an absolute guarantee claim, particularly where, as here, the ads make no mention of any condition on actual use. Indeed, the ads stress the fact that the flashlight works "when you need it." Even if few consumers would believe the light could stay on continuously for five years—an assumption that stretches credulity—they might well conclude that it should work under abnormal as well as normal patterns of usage. Consequently, we concur with the ALJ that, absent disclosure of the "on-life" conditions, respondents' claims for their flashlight had the capacity to mislead purchasers. [17]

D. *Lincoln Penny* Respondents also sell a collector's Lincoln penny bearing the likeness of former President Kennedy. The ALJ found that respondents misrepresented that:

> Their Lincoln-Kennedy penny was minted by the United States Treasury Department;
>
> Their Lincoln-Kennedy penny is a coin of historical and numismatic significance which is certain to grow in value;

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[14] Based on evidence stipulated to at trial, normal usage of a flashlight is about two hours per year, or 10 hours over a five-year period. (ID 46)

> The issuance of their Lincoln-Kennedy penny was sanctioned by Section [331], Title 18 U.S. Code; and
>
> A free plaque containing historical coincidences between the lives of President Lincoln and President Kennedy is provided to purchasers with each coin. (ID 47)

On February 27, 1974, prior to issuance of the instant complaint, the United States Postal Service ruled that respondents had made misrepresentations similar to those set forth above in connection with the advertising of the Lincoln-Kennedy penny and issued an order limiting the postal services thereafter available to respondents. (ID 47)

Respondents have not sought to relitigate the substantive issues in this matter. Rather they urge on appeal that the allegations should be dismissed as not being in the public interest because the Postal Service decision adequately addresses the deception found in their advertising of the so-called "Lincoln-Kennedy" penny. Indeed, respondents argue that the challenged advertising was terminated even before the Postal Service issued its order. Abandonment of the practices, however, is no defense here. As complaint counsel point out, the present action involves claims made after as well as before issuance of the 1974 Postal Service order. (CAB at 35-36; CX 275, 405 at 11) A review of these later ads reveals that respondents have continued to misrepresent the source and value of the Lincoln-Kennedy penny. [18]

Furthermore, we reject respondents' contention that this case against the Lincoln-Kennedy penny lacks public interest. We note that the complaint issued in this case on September 3, 1975—well after the Postal Service issued its order against respondents. Recently, this Commission faced a similar contention that an already litigated case lacked public interest. *See Porter & Dietsch,* Dkt. 9047, slip op. at 32, 90 F.T.C. 770, (1977). There we noted that respondents' contention of a failure for want of public interest implicitly rests on "the wisdom of using limited public resources to correct particular law violations, a decision committed to the Commission's discretion." *Id.* Our response in that case applies with equal force here, "that bridge was crossed for the last time over two years ago when the Commission issued the complaint in this case." *Id.*

Finally, we concur with the ALJ's determination concerning respondents' offer of a "free" plaque (or resume) of historical coincidences.[15] The evidence indicates that over a period of years the

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[15] There is no merit in respondents' contention that they lacked proper notice of this issue. Paragraphs 9-11 of the complaint clearly refer to the claims at stake here. There is also no foundation for respondents' assertion that litigation of this issue borders on harassment because it is inconsequential and could have been litigated in the

(Continued)

plaque and coins were never offered at a different price. (CX 62, 66, 69, 275)[16] By advertising a "free" plaque, Jay Norris presumably hoped to convince consumers that the package deal was a bargain, [19] *i.e.,* that the penny was competitively priced and for a limited time the plaque would be tossed in for no additional charge. The deceptive potential of a "free" offer which is not *bona fide* is well established. *See FTC* v. *Mary Carter Paint Co.,* 382 U.S. 46 (1965); *Kalwajtys* v. *FTC,* 237 F.2d 654 (7th Cir. 1956), *cert. denied,* 352 U.S. 1025 (1957). *See also F.T.C. Guide Concerning Use of Word "Free" and Similar Representations,* 16 C.F.R. 251 (1971). While the consumer injury here may not be great, we find the inclusion of such a representation in respondents' ads to be false and misleading, absent any evidence that the plaque was genuinely offered at no charge.

E. *Antenna* In connection with their advertisements for this product, respondents were found to have represented that: (1) the TV antenna will bring sharp and clear reception even in difficult areas; (2) the performance of the antenna is superior to any rabbit ear antenna or outdoor antenna; (3) the device will turn all types of house wiring into a TV antenna; and (4) their antenna is an electronic miracle (ID p. 45). Upon reviewing the evidence (CX 28, 886) we believe there can be little doubt that respondents' advertisements make these representations. For example, a typical ad (CX 886) includes the following assertions:

> every home a super receiver,
>
> one of the greatest TV antennas ever constructed,
>
> a super receiver for black and white TV, FM, all kinds of difficult reception,
>
> electronic miracle,
>
> better than any set of rabbit ears, more efficient than complicated external antennas,
>
> reception so sharp and clear it will amaze you even in more difficult areas.

[20] Though they did not contest having made such claims, respondents contend that the evidence adduced is insufficient to establish the falsity of these representations. Respondents again question the probative value of the consumer testimony elicited here, observing that these consumers are neither television nor antenna experts and, therefore, might not know when a television or antenna

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earlier Postal Service action. Neither the circumstances of this case nor the decision in *Sunshine Anthracite Coal Co.* v. *Adkins,* 310 U.S. 381 (1940), which respondents cite, provides any basis for such an argument.

[16] Since the two items apparently were never sold separately, the only issue is whether they were ever sold at a higher, or regular price.

installation was defective (RAB at 39–40). Yet, the consumers expressing dissatisfaction with the Jumbo Antenna had working television sets which operated well before and after the use of respondents' product (Tr. 334–335, 469). While it is possible these consumers improperly installed the Jumbo Antenna, this possibility appears remote. (Tr. 468–469)[17] In our view, this consumer testimony is persuasive evidence of the falsity of respondents' representations.[18]

Additionally, we find that witness Triolo's tests of respondents' product and other antennae provide convincing independent evidence that the expansive representations for the Jumbo TV Antenna are false. Mr. Triolo, who has thirty years' experience with technical antennae (Tr. 271), tested each of three types of antennae: an outdoor antenna, rabbit ears, and respondents' product (Tr. 273–274). At each of the two test sites, both the outdoor antenna and rabbit ears produced significantly better pictures than did the Jumbo TV Antenna (CX 2704). [21]

Respondents challenge Mr. Triolo's expertise, the reliability of his methods, and his impartiality. First, we find it irrelevant whether Mr. Triolo is a television expert. As we have already observed, even a layman can determine whether the TV picture is relatively the same before and after the installation of different antennae. Further, Mr. Triolo has the relevant expertise required in these tests: the ability to connect and disconnect the various antennae properly (Tr. 271).

Respondents also attempt at length to discredit Mr. Triolo's tests as unscientific or inconclusive for purposes of this proceeding. They fail. Respondents claim amazing performance even under the most difficult conditions; they also assert that their product is better than any set of rabbit ears and more efficient than complicated outdoor antennae. It is clear from an examination of the pictures taken in the course of the tests that respondents' product consistently produced substantially inferior television receptions compared to those produced by the other antennae. (CX 2704L–X) Respondents on the other hand have offered no substantial evidence to back up their claims.

Finally, respondents challenge Mr. Triolo's impartiality because he conducted the tests at the behest of Mrs. Mulhern, a Commission employee (Tr. 272–275), The record contains no evidence that would suggest that Mr. Triolo was anything but objective (*Id.*). Certainly the mere fact that the Commission staff has contracted for a study does not undermine the study's conclusions. Although Mr. Triolo's tests were limited in nature,[19] we believe they adequately demonstrate the falsity of respondents' broad claims.[20] [22]

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[17] One of the witnesses was an experienced electronics design engineer. (Tr. 468–469) Moreover, respondents tout the ease of installation in their ads, advising consumers that "no special tools or additional material [is] required" and "you simply attach the adapter easily and quickly to your set. . . . (CX 886)

[18] Respondents place considerable reliance on the testimony of Mrs. Theodora Pierce who expressed satisfaction with respondents' antenna (RX 9A, B). While such testimony tends to prove that respondents' product in fact operates as an antenna, it does not rebut the experience of other consumers that the antenna fails to perform as claimed.

F. *Ex-Taxis* For approximately five years from 1969 to 1974, respondent Pan Am engaged in the rather creative venture of selling through the mails used New York City taxicabs. Some 700–800 cars were sold during this period. As the ALJ found, respondent's advertising contained a host of misrepresentations concerning the mechanical and physical condition of these cars as well as their availability. In addition, the ALJ determined that the failure to disclose where the taxis came from and that the interiors of the cars were not reconditioned had the tendency and capacity to deceive prospective customers.[21] Respondents take issue only with the findings of non-disclosure.[22]

Undoubtedly, anyone who has had the scintillating experience of riding in a New York City taxicab — and presumably many who haven't but who have heard the tales related by others — will realize that these cars frequently do not receive the most delicate treatment. Nevertheless, we are reluctant to single New York out for special mention as the locale where these taxis saw service. While the trials and tribulations may be greater there, we suspect that conditions are not so different elsewhere that mere disclosure of the fact that the cars being offered for sale were once driven as taxis should suffice to alert would-be purchasers to the risks involved. Since respondent's ads disclosed that the used cars were ex-taxis, we decline to go further. [23]

Nor are we persuaded that this record adequately demonstrates the need for disclosing whether the car interiors have been cleaned or reconditioned. The ALJ did not find that respondent misrepresented the interior condition of the cars (ID pp. 56–57); neither do we. Although a mail order purchaser might reasonably expect that the car interiors were in presentable shape, it is also likely that most consumers would expect a used car, particularly a used taxi, to show signs of wear. Beyond that, the record is inadequate to establish that the interiors were generally in such poor condition that disclosure of that fact in respondent's advertising should be required.[23]

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[19] Respondents also object to a number of other methodological factors (RAB at 42–43), but we believe they do not undercut the essential validity of the results.

[20] Respondents also urge that their use of the phrase "Electronic Miracle" is mere puffery. Although not insensitive to respondents' concern that the term "miracle" is commonly used in situations short of changing water into wine, we must conclude that the use of "electronic miracle" in the context of respondents' grossly exaggerated claims would lead consumers to give some added credence to the overall suggestion that this device is superior to other types of antennae.

[21] Finding insufficient record support, the ALJ dismissed allegations concerning claims relating to the appearance and price of the cars and the responsibility for effecting delivery. (ID p. 56) Similarly, the law judge dismissed allegations that respondents failed to disclose the meaning of "FOB" and "as is," whether the cars complied with any state motor vehicle inspection law, and whether the drivers hired to deliver cars to purchasers were independent contractors (ID p. 57).

[22] Respondents' other objection concerns paragraph I 3, which would require their automobiles to meet the various state inspection requirements and is considered in the discussion on relief.

Moreover, aside from proscribing future misrepresentations, neither the notice order nor the order proposed by the law judge would require respondents to disclose the mechanical condition of their cars. The record reveals, however, that this attribute of the cars caused consumers the most trouble. We are reluctant to require the more intrusive remedy of affirmatively disclosing the condition of the car interior where the evidence of materiality is much less compelling. However, should respondents be induced to get into the used car business again, we believe the order provisions appropriately fence-in respondents with respect to misleading claims concerning a car's physical condition (both exterior and interior) as well as its mechanical condition. [24]

IV. *Unfair Business Practices*

The complaint alleged several additional unfair practices, including retention by respondents of monies for merchandise not shipped promptly, maintaining an unlisted telephone number and requiring proof of purchase and/or proof of return shipment in cases of nondelivery and demands for refunds.[24]

There is no dispute with the ALJ's determination that respondents committed an unfair practice in retaining customer payments while not fulfilling their end of the bargain by making prompt deliveries and refunds as promised. It is no less unfair for a firm to keep the benefits of unlawful acts than it is to have engaged in those acts in the first place. *See Koscot Interplanetary, Inc.*, 86 F.T.C. 1106, 1157, 1184-85 (1975); *Universal Credit Acceptance Corp.*, 82 F.T.C. 570, 647-54 (1973), *rev'd in part sub nom. Heater* v. *FTC* (refund provisions set aside), 503 F.2d 321 (9th Cir. 1974); *cf. Windsor Distributing Co.*, 77 F.T.C. 204, 222-23 (1969), *aff'd*, 437 F.2d 443 (3d Cir. 1971).

As for the unlisted telephone, the ALJ found that it was not unfair for respondents to close off this form of communication since other means were available. (ID p. 63) But once a customer complains about nondelivery or a failure to refund, the ALJ held it to be an unfair practice for respondents not to provide the customer with a telephone number for future contacts. (ID p. 65)

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[23] What consumer testimony the record contains on this point sheds little light as to what consumers expected. One consumer, although disappointed, found the interior satisfactory (Tr. 1118-1119). Two others objected to the interior being dirty (Tr. 1102, 1138), but it is not clear whether this dirt would be easily removed. And another consumer objected to the fact that the dash was taped where the taxi equipment had been removed (Tr. 1178).

[24] A separate charge that respondents used numerous corporate names unfairly to create confusion in consumers' minds was dismissed by the law judge. (ID 41)

We sympathize with the plight of consumers who have been frustrated in their attempts to obtain satisfaction from respondents. Similar problems were extensively documented during the Commission's consideration of the mail order rule. (*See* 40 F.R. 51582–86 (1975)) Nevertheless, we agree with the ALJ that many of the same difficulties encountered by purchasers in communicating with respondents by writing are likely to crop up in telephone contacts. (*See* ID p. 64) By correcting the central problem surrounding respondents' operations, namely their failure to perform as promised, many of the difficulties involved in [25] resolving complaints can be cleared up. That is the objective of our order as well as the mail order TRR (which also contains no telephone disclosure requirement). Moreover, for many customers of Jay Norris, telephone access would be of little value since the low price of many of the items purchased would not justify the cost of a long-distance call to the company's New York offices.

Thus, we concur in the law judge's refusal to require respondents to list their telephone number. For similar reasons, we decline to follow the ALJ's ruling concerning respondents' failure to disclose their phone number when responding to complaints.

The ALJ further concluded that in certain cases respondents unfairly required customers to submit proof of purchase before complaints were acted upon. This allegedly was necessitated by respondents' failure to keep better records. (ID p. 64) In reaching this decision the law judge rejected respondents' attempt to analogize their practice to the requirements customarily imposed by retail stores. He noted that

> a retail store which provides a sales slip and a face to face confrontation between the customer and the seller . . . is in a different situation than a mail-order business that sells merchandise unseen, prepaid, by mail. As long as respondents represent that the customer will get a refund or that delivery is guaranteed, they cannot require proof of payment, as a condition for their acting on a complaint, unless they disclose to the customer in the original contact that such proof will be required before reshipment or refund is made. (*Id.*)

However, the ALJ's finding of unfairness appears to be based on respondents' recordkeeping deficiencies, rather than the fact that they demanded proof of payment before making a refund or reshipment.

We agree with the law judge that customers ordering by mail should be able to expect that their orders could be satisfactorily processed by respondents in the ordinary course of business without the need for further documentation. But the record here clearly does not support the charge that respondents systematically demanded proof of purchase before granting a refund or reshipping the ordered merchandise. To [26] be sure, respondents at one time used a form letter in responding to complaints which requested further information, such as the date of original order, the product ordered and the amount of the check. (CX 4245) Mr. Williams, vice-president and treasurer of Jay Norris, testified, however, that this form was employed only in those instances in which the customer didn't provide sufficient information for respondents to "check it back." (Tr. 196) Moreover, at some indeterminate time in the past respondents even stopped requesting this kind of information and simply shipped the customer duplicate merchandise where sufficient time had elapsed for delivery. (Tr. 196; CX 4248)

In view of this evidence we cannot sustain the law judge's finding that respondents' practices were unfair. Nor do we retain the recordkeeping provisions in paragraph 20 of the ALJ's order designed to remedy these alleged practices. To the extent better records are required, we believe the provisions of the mail order rule (which we incorporate in this order), together with the requirement for retention of complaint correspondence, satisfactorily address the shortcomings in respondents' recordkeeping procedures.

V. *Relief*

The order proposed by the ALJ differs in a number of respects from the original notice order. As discussed more fully below, we adopt with revisions the basic approach reflected in the law judge's recommended order.

A. *Delivery and Refund Practices* Both the notice order and the ALJ's proposed order rely primarily on provisions drawn from the Mail Order Merchandise TRR to remedy the violations uncovered in connection with respondents' delivery and refund practices.[25] Though the findings made in a specific case may justify harsher or milder remedies than those applied industrywide, we are persuaded that the law judge properly incorporated large portions of the mail order rule in his order. That is because many of the [27] problems encountered by consumers in this case are similar to those which led to issuance of the Rule and because we are challenging largely pre-TRR practices. Thus, in the absence of any particularly unique conditions in this proceeding, we are reluctant to stray from the guidance provided by the Rule.

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[25] The corresponding provisions in the order we issue are Paragraphs 3-5 of Part I. Paragraph 1, as modified, addresses respondents' practice of not making prompt refunds for merchandise returned. Paragraph 2 remedies the failure to refund all monies including shipping costs.

Indeed, in view of this situation, we believe it is appropriate to reinstate in our order the rebuttable presumptions contained in the TRR but deleted from paragraphs 4(c) and 5(c) of the order recommended by the ALJ. Under the Rule mail order sellers without documentary proof are presumed to lack a reasonable basis for their delivery claims. (16 C.F.R. 435.1(a)(4)) Similarly, sellers are presumed to have failed to provide buyers with an adequate opportunity to exercise their rights in the event of a delayed delivery by not providing written notification or the means to reply in writing. (*Id.* 435.1(b)(3)) However, the Commission permitted mail order firms to overcome these presumptions by demonstrating that equally effective means were used to meet the TRR's objectives.[26]

We see no compelling basis to depart from that scheme here. To be sure, respondents' meager recordkeeping contributed to our finding that they failed to live up to the performance claims in their advertising. Respondents clearly will have to limit their claims to the performance they can deliver. Moreover, it appears obvious that they will have to improve their procedures in order to conform with the requirements of this order and the Rule. For example, respondents will have to show that ordered merchandise is shipped routinely within the time promised (or if no time is specified within 30 days) and that procedures are in place which assure that purchasers are properly notified of shipping delays. Respondents' present inability to ascertain [28] when, or whether, shipment has been made following receipt of an order cannot continue.[27] Nevertheless, we are not disposed to foreclose alternative means of compliance so long as they satisfy the standards of conduct set forth in the order. In short, we believe reliance on the mail order rule as a basis for this part of the order provides a fair and effective means for dealing with the practices found unlawful in this proceeding.[28]

B. *Substantiation Requirements* Respondents challenge virtually every provision in the ALJ's proposed order, but nowhere is their opposition more vehement than that directed against order paragraph I 7 which prohibits them from:

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[26] As the Commission recognized in that proceeding, care must be taken not to unduly restrict the ability of companies attempting to deliver goods to consumers in the most cost-effective manner. [*See, e.g.*, 40 F.R. at 51588 (potential cost of recordkeeping), *Id.* at 51589 (flexible requirements on seller depending on number of delays), *Id.* at 51590 (30-day grace period to obtain buyer's consent).] We appreciate the fact that some improvements in the reliability of performance may exact too high a cost in reduced efficiency and higher prices.

[27] The only records kept were the (1) customers' names and addresses, (2) the date the order was received, (3) the amount of money remitted, and (4) for noncatalog orders, the product purchased. (ID 21) No records are kept showing shipment dates for specific orders.

[28] Another advantage of incorporating the mail order rule provisions in this order is that the explanations and interpretations associated with the Rule will facilitate compliance with the order.

> Representing the safety, efficacy, performance, content, or any other characteristic of any product unless such claims are fully and completely substantiated by a reasonable basis which shall consist of competent objective material and substantiative material is available to the public. (ID pp. 86–87)

Respondents contend that paragraph I 7 infringes on their First Amendment rights, exceeds the Commission's statutory authority, and fails for lack of public interest. We consider each of these contentions in turn. [29]

It is beyond dispute that commercial speech is protected by the First Amendment. *See Bates* v. *Arizona*, 433 U.S. 350 (1977); *Virginia State Board of Pharmacy* v. *Virginia Citizens Consumer Council, Inc.*, 425 U.S. 748 (1976); and *Bigelow* v. *Virginia*, 421 U.S. 809 (1975). It is equally clear, however, that commercial speech does not enjoy the same unfettered protection as political speech. In particular, deceptive or misleading commercial speech is properly subject to government regulation. For example, as the Court observed in *Virginia Pharmacy*,

> much commercial speech is not provably false, or even wholly false, but only deceptive or misleading. We see no obstacle to a State's dealing effectively with this problem. (*Id.* at 773; *see also, Bates*, 433 U.S. at 383–84)

More recently, in ***Ohralick*** v. ***Ohio State Bar Association***, the Supreme Court explained why commercial speech is differentiable from other protected speech:

> To require a parity of constitutional protection for commercial and noncommercial speech alike could invite dilution, simply by a leveling process, of the force of the Amendment's guarantee with respect to the latter kind of speech. Rather than subject the First Amendment to such a devitalization, we instead have afforded commercial speech a limited measure of protection, commensurate with its subordinate position in the scale of First Amendment values, while allowing modes of regulation that might be impermissible in the realm of noncommercial expression. [46 USLW 4511, 4513–14 (1978)]

Respondents contend, though, that this order prohibits them from making representations for which they have no reasonable basis but which are nonetheless true. (RAB at 4–10) Complaint counsel counter by arguing that the order constitutes a reasonable deterrent to future deceptive advertising by proven violators of the FTC Act. (CAB at 7) [30]

In the first place, there is nothing novel about the substantiation provisions contained in this order. Similar requirements preventing sellers from disseminating advertisements without having a reasonable basis for their claims have been included in numerous Commission orders.[29]

Moreover, while we are sensitive to Constitutional implications in fashioning a proper remedy for deceptive advertising, where the Commission merely orders violators to reasonably substantiate their performance claims, as it does here, such a requirement furthers rather than impairs First Amendment objectives. As the Seventh Circuit explained in *National Commission on Egg Nutrition, et al.*, 570 F.2d 157, 162 (7th Cir. 1977), *petition for cert. filed*, 46 USLW 3694 (April 28, 1978), the First Amendment interest in commercial speech also embraces the interests of the prospective audience - consumers. The consumers' interest in product information "is served by *insuring* that the information is not false or deceptive, and in fact, coincides with the public interest served by the regulation." (*ID.*) (emphasis added) The Supreme Court has also recognized the importance in insuring that commercial speech flows cleanly, commenting in *Bates* that

> the public and private benefits from commercial speech drive from confidence in its accuracy and reliability. Thus the leeway for untruthful or misleading expression that has been allowed in other contexts has little force in the commercial arena. (433 U.S. at 383–84)

Of course, concern for accuracy in commercial speech is not a new one for this Commission. In *Porter & Dietsch*, we recently considered how our statutory obligations to prohibit deceptive commercial speech mesh with the objectives of the First Amendment: [31]

> Deceptive commercial speech does not aid consumers in making their purchasing decisions and may cause economic injury to those consumers who purchase the advertised product because of the deception. It also reduces the effectiveness of all advertising by casting doubt on its reliability. Therefore, although sensitive to the public interest in the free flow of commercial speech, we serve the same public goals when we meet our statutory obligations by prohibiting deceptive advertising. (Slip op. at 5)

Similarly, in *Egg Nutrition*, we stated:

> Neither the objectives of the First Amendment, nor of the FTC Act are well-served, however, by commercial speech which is deceptive *** As Justice Stewart noted in concurring with the majority in *Virginia Pharmacy Board*, "*** the elimination of false and deceptive claims serves to *promote* the one facet of commercial price and product advertising that warrants First Amendment protection — its contribution to

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[29] *See e.g., Porter & Dietsch*, slip op. at order paragraphs I. A and I. B. [90 F.T.C. 770]; *Fedders Corp.*, 85 F.T.C. 38, 69 (1975), *aff'd*, 529 F.2d 1398 (2d Cir. 1976), *cert. denied*, 429 U.S. 818 (1976); *National Dynamics Corp.*, 82 F.T.C. 488, 569 (1973), remanded for other reasons, 492 F.2d 1333 (2d Cir. 1974), *cert. denied*, 419 U.S. 993 (1974); *Firestone Tire & Rubber Co.*, 81 F.T.C. 398, 475 (1972), 481 F.2d 246 (6th Cir. 1973), *cert. denied*, 414 U.S. 1112 (1973).

> the flow of accurate and reliable information relevant to public and private decisionmaking." [425 U.S. at 781] (88 F.T.C. at 196) (emphasis added)

Respondents' argument appears to stem from the fear that the cost of acquiring a reasonable basis which they feel confident meets the order's requirements will chill their dissemination of truthful advertising claims. Yet, as the previously cited decisions emphasize, more reliable information enhances the flow of truthful advertising and furthers First Amendment interests. Since advertisers are in a far better position than consumers to verify the accuracy of their claims, it is only reasonable that they bear the burden of such verification.

Moreover, as the Commission has held on prior occasions, representations of objective product characteristics made without substantiation are, *for that reason,* deceptive, *National Dynamics Corp., et al.,* 82 F.T.C. 488, 559-60 (1973); *aff'd,* 492 F.2d 1333 (2d Cir.), *cert. denied,* 419 U.S. 993 (1974). Accordingly, when it forbids unsubstantiated performance claims by way of fencing in, the Commission is doing no more than proscribing a class of *deceptive* claims—indisputably permissible action under the First Amendment, *Virginia State Board of Pharmacy* v. *Virginia Citizens Consumer Council, Inc.,* 425 U.S. 748, 771 n. 24 (1976). [32]

In *Egg Nutrition,* the Commission observed that

> Many consumers are likely to assume that when a product claim is advanced which is in theory subject to objective verification, the party making it possesses a reasonable basis for so doing, and that the assertion does not constitute mere surmise or wishful thinking on the advertiser's part. As a result, the rendition of a claim based upon inadequate or nonexistent substantiation violates Section 5 for failure to state a highly material fact, whose omission is deceptive. (88 F.T.C. at 191)

Although the complaint did not include such a charge, as respondents point out (RRB at 4), requiring them to have substantiation for their claims is clearly an appropriate remedial device for preventing recurrences of deceptive advertising.[30] [33]

As the Supreme Court has pointed out, the hardiness and objectivity of commercial speech make the prospects of its being chilled by proper regulation unlikely. *Bates,* 433 U.S. at 383–84; *Virginia Pharmacy,* 425 U.S. n. 24 at 771–72' These attributes led the court in *Virginia Pharmacy* to indicate that earlier cases approving the reasonableness of regulatory prior restraints on commercial speech have continuing validity. *E.g., Donaldson* v. *Read Magazine,* 333 U.S. 178, 189–191 (1948); *FTC* v. *Standard Education Society,* 302 U.S. 112 (1937); *E. F. Drew & Co.* v. *FTC,* 235 F.2d 735, 739–740 (2d Cir. 1956), *cert. denied,* 352 U.S. 969 (1957).[31] And elsewhere the Supreme Court has noted as well established the Commission's power to restrain misleading statements in labels and advertisements. *See Young* v. *American Mini Theatres, Inc.,* 427 U.S. 50, 69 n. 31 (1976).[32] *See also Ohralick,* 46 USLW at 4513–14.

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[30] We also note that it appears the Commission would be fully justified under the circumstances of this case in imposing upon respondents a broad requirement that they not *misrepresent* the safety or performance of any of the products they sell. For example, the Commission has entered, and courts have sustained, orders forbidding broad categories of misrepresentations with respect to the sale of "all products," *see American Aluminum Corporation, et al.,* 84 F.T.C. 21 (1974), *aff'd,* 522 F.2d 1278 (5th Cir. 1975); *All State Industries of North Carolina, Inc.,* 75 F.T.C. 465, 495 (1969), *aff'd,* 423 F.2d 423 (4th Cir.), *cert. denied,* 400 U.S. 828 (1970); *Mutual Construction Co., Inc., et al.,* 87 F.T.C. 621 (1976). We choose here not to enter an order prohibiting misrepresentations of various facets of all respondents' products; respondents will not be held to account for the absolute truth of their claims. Thus we impose a lesser remedy by requiring that respondents not make a safety or performance claim for any product without a reasonable basis. Rather respondents must simply substantiate these claims, and this will absolve them of civil penalty liability should any claim ultimately be proven false—clearly an unexceptionable approach under the First Amendment.

Undoubtedly, many advertisers, irrespective of a substantiation requirement, would take steps to document their claims as a matter of good business practice or possibly out of fear of a subsequent false advertising challenge. To that extent, truthful advertising will not be chilled. Though substantiation increases the risk that some truthful, as well as false, claims may be challenged, it is a small price to pay to insure greater confidence in all [34] advertising. Whatever incremental reduction in advertising, attributable to a substantiation order, beyond that which would result if advertisers only disseminated nondeceptive claims "may well be necessary if the interest of consumers in truthful information is to be served at all." *Warner Lambert* v. *FTC,* supp. op. 1977-2 Trade Cases p. 61,646 at 72,653 (September 14, 1977), *cert. denied,* 46 USLW 3613 (April 4, 1978). *See also National Society of Professional Engineers* v. *U.S.,* 98 S. Ct. 1355, 1365–68 (1978).

Respondents also advance several additional arguments to the effect that paragraph I 7 of the ALJ's order exceeds the scope of the Commission's authority: (1) the coverage of all products and any advertisement is too broad, (2) the standard of "full," "complete" and "competent" substantiation is too vague, and (3) the requirement of making substantiative material generally available to the public is unwarranted.

Regarding the "all products – any advertisement coverage," respondents stress that the proposed order is overly broad and unduly burdensome. Respondents, however, have previously been subjected to orders of the Commission, the U.S. Postal Service and the New York State Attorney General for claims for three different products.[33] Moreover, in this case we have found that respondents misrepresented the performance of six products of widely varying cost and use. [35] The Commission has authority to fashion broad relief where necessary to deal effectively with wrongdoers. *See Firestone Tire & Rubber Co.,* 81 F.T.C. 398, 468 (1972), 481 F.2d 246 (6th Cir. 1973), *cert. denied,* 414 U.S. 1112 (1973) and cases cited therein.[34] The Commission's order must, or course, be tailored in some measure to the violations found. But where, as here, the violations involve a wide variety of products and a wide variety of deceptive claims an effective order must necessarily be very broad. That is particularly true in light of the history of prior proceedings undertaken to prevent deceptive claims by respondents. Precisely because they sell so many products, with no one category being substantially more important than any other, it seems likely that an order which did not apply to all products would do very little to protect the public. Rather than eliminating future deception, it would merely shift its locus to a different part of respondents' catalog.[35]

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[31] *Virginia Pharmacy* and *Bates* also leave intact other Commission cases holding that the government can restrict commercial speech to prevent deception to consumers, citing *Tashof* v. *FTC,* 437 F.2d 707 (D.C. Cir. 1970); *Murray Space Shoe Corp.* v. *FTC,* 304 F.2d 270 (3rd Cir. 1962); *American Medicinal Prods. Inc.* v. *FTC,* 136 F.2d 426 (9th Cir. 1943). In *Tashof,* the court upheld a Commission order prohibiting a retailer from advertising discount prices without first conducting a "statistically significant survey" of competing stores to establish the accuracy of its claims. Even though the court conceded that advertised prices might otherwise be truthful, it found the requirement of a prior survey to be a reasonable deterrent to future violations. (347 F.2d at 715)

[32] The Court relied on *Jacob Siegel Co.* v. *FTC,* 327 U.S. 608 (1946); *FTC* v. *National Commission on Egg Nutrition,* 517 F.2d 485 (7th Cir. 1975); *E. F. Drew & Co.* v. *FTC,* 235 F.2d 735, 740 (2d Cir. 1956).

Although the order is broad, we note that respondents' troubles stemmed in large measure from making unqualified claims which, at least in the case of the flashlight and roach powder, overstated the manufacturers' claims for the products. By exercising a little more care in preparing their ads, respondents' compliance burdens under this order will be greatly reduced. Moreover, we have modified the substantiation provision in Part I of our order to limit its coverage to safety and performance claims, thereby [36] deleting reference to content or other product characteristics.[36] This change appropriately narrows the scope of the provision to those kinds of deceptive claims which predominate in this case. Additionally, we have clarified the order to provide that substantiation must be available in written form. For example, that does not preclude respondents from relying, where appropriate, upon the technical advice of qualified persons for substantiation of product claims. It only means that such advice must be reduced to writing.

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[33] The order issued by the Commission in this matter will be the third imposed by the Commission upon these respondents within the past 15 years. The first order, a consent settlement, forbade various misrepresentations concerning the nutritional characteristics of vitamins and vitamin-mineral preparations, *Jay Norris Company Trading as Norris Nutritions, et al.*, 68 F.T.C. 702 (1965). The second order was entered after litigation and involved misrepresentations by respondents regarding their trade status and deceptive pricing, *Federated Nationwide Wholesalers, et al.* v. *Federal Trade Commission,* 398 F.2d 253 (2d Cir. 1968. *See also* U.S. Postal Service proceeding as referred to in ID 47; and Assurance of Discontinuance Pursuant to Executive Law Section 63, Subdivision 15, Attorney General of the State of New York Bureau of Consumer Frauds and Protection, dated June 30, 1976.

[34] *See also FTC* v. *Colgate Palmolive Co.,* 380 U.S. 374, 392 (1965); *Jacob Siegel Co.* v. *FTC,* 327 U.S. 608, 613 (1946); *Warner Lambert Co.* v. *FTC,* 562 F.2d 749, 762 (7th Cir. 1977), *cert. denied,* 46 USLW 3613 (April 4, 1978); *Niresk Industries, Inc.* v. *FTC,* 278 F.2d 337, 343 (7th Cir. 1960), *cert. denied,* 364 U.S. 883, cases which limit the Commission's discretion only by requiring that the remedy be reasonably related to the unlawful practice.

[35] No logical sub-grouping of respondents' products is suggested as a basis for limiting product coverage and there appears to be none. Respondents' products generally, like the ones involved in this case, vary tremendously in price and use. In any event, this record demonstrates that respondents' penchant for misrepresentation of performance is not confined to a narrow sub-group of products they sell.

[36] Performance claims clearly encompass representations as to efficacy.

A separate substantiation provision has been inserted in Part II of the order to avoid any suggestion that the reference to "any product" in paragraph 6 of Part I does not include products covered by Part II. Part II coverage also has been expanded to include all used motor vehicles, rather than just automobiles, Given the variety and seriousness of the misrepresentations which occurred in connection with respondents' sale of used cars, it seems appropriate to fence in respondents as to future mail order sales of other types of vehicles, such as trucks, motorcycles, campers and the like.

Respondents further contend that the broad standards provided by the words "full," "complete" and "competent" are unduly vague and illegal as a matter of law. We note that similar language has been used in other substantiation orders. *See* n. 29, *supra.* These cases provide ample guidance to respondents in construing these terms, and more generally, the concept of reasonable basis. Moreover, we believe that the general meaning of these terms is readily understood.

Respondents next question the legal basis for requiring substantiation to be generally available to the public. We do not reach this question because we find there has been no showing that this is necessary to cure the violations found to exist. In this context it is sufficient that consumers are in a position to rely on the advertising claims without the trouble and expense of investigating the substantiation for themselves. *See Porter & Dietsch,* slip op. at 38. [37]

Finally, relying on *NLRB* v. *Wyman Gordon Co.,* 394 U.S. 759 (1969), respondents contend that prior substantiation requirements should be addressed in a rule forum. We recently rejected "this variation on the old theme of selective enforcement." *Porter & Dietsch,* slip op. at 32. We reject it again. We do not believe the public good would be well served if the Commission, in dealing with proven violators of Section 5, refrained from meeting out in administrative proceedings remedies appropriate to the violations found. Moreover, under 15 U.S.C. 45(m), the Commission is free to hold other concerns to the same standards we are imposing on these respondents, when the order we will enter becomes final.

Thus, having rejected respondents' challenges to the propriety of requiring them to substantiate their claims, the final order will include such a provision.

C. *Other Provisions* After excising those order provisions for which corresponding violations were not found,[37] we adopt with some revisions the ALJ's order as it applies to the specific misrepresentations involving the six products.

In addition, we delete paragraph I 3 of the law judge's order which would prohibit respondents from shipping to any state any car which fails to meet the motor vehicle registration, safety and inspection standards of that state. The ALJ retained this provision in the order without explanation after dismissing the complaint charge that respondents failed to disclose a material fact by not revealing whether their cars were inspected for compliance with state law. [38] (ID p. 57) The record sheds little light on respondents' obligations under state inspection laws, the extent of their compliance with such laws, or whether state law is adequate to deal with the kind of distribution scheme engaged in by respondents. Thus, absent deception, we find little basis for imposing this requirement.[38]

We also believe paragraph I 13 of the proposed order is somewhat overbroad. Our determination that respondents deceptively advertised their roach powder as safe is based on the failure to qualify such claims by noting that the product could be used safely only in accordance with the instructions on the label. A more appropriate disclosure requirement is to require respondents to condition any claim of safety in ads for pesticides by including the following language: "To Use This Product Safely, You Must Follow The Instructions On The Label."

Lastly, we agree that the ALJ properly included Jay Norris, Jacobs, and Williams within the scope of Part II of the order.[39] The law judge's discussion of this issue is persuasive (ID p. 58). Jacobs and Williams were stockholders and corporate officers of Pan Am (*Id.;* Tr. 163). Though these individual respondents may not have taken an active role in the day to day business of Pan Am (Tr. 155, 167), they clearly were aware of its operations (Tr. 159, 167). *See Standard Educators, Inc.* v. *FTC,* 475 F.2d 401 (D.C. Cir. 1973), *cert. denied,* 414 U.S. 828 (1973). Furthermore, Pan Am's business was conducted by Norris personnel at the Norris place of business (*Id.;* CX 752–754, 756). [39]

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[37] Those provisions dropped include (1) disclosure of the roach powder ingredients, (2) disclosure of the interior condition of respondents' used cars, and (3) disclosure that the taxis were from New York.

[38] Respondents' ads do assert that "[e]ach car has been thoroughly serviced by our mechanics to put it in good operating condition and passes careful inspection before being released for delivery." *See, e.g.,* CX 51A. Although, as the ALJ noted (ID p. 57), it is not entirely clear what this "inspection" refers to, we are reluctant to construe it as meaning that respondents' cars conform to the inspection requirements of all 51 jurisdictions. Nor does the complaint allege such a claim. (*Cf.* complaint para. 9(21))

[39] With respect to Part II of the ALJ's order, respondents contend and the complaint counsel agree that the first word of paragraph 2 should be "misrepresenting" rather than "representing" (RAB at 50; CAB at 39). We have retained this provision in the final order as so modified.

For reasons already articulated, the final order will not include provisions requiring respondents to disclose the Norris telephone number in response to complaints and imposing on them specific recordkeeping responsibilities. (*See* paragraphs I 19 and I 20 of the ALJ's order) We have kept in the final order, however, the provision obligating respondents to maintain records of consumer complaints, including the disposition of such complaints, for three years. This information is necessary to assist the Commission in ascertaining compliance with the order. To the same end, we have also inserted a requirement similar to that contained in other orders that respondents submit a detailed compliance report within 60 days and annually thereafter for five years.

FINAL ORDER

This matter having been heard by the Commission upon the appeal of respondents from the initial decision, and upon briefs and oral argument in support thereof and opposition thereto, and the Commission for the reasons stated in the accompanying Opinion having determined to sustain the initial decision with certain modifications: [2]

It is ordered, That the initial decision of the administrative law judge, pages 1–73, be adopted as the Findings of Fact and Conclusions of Law of the Commission, except to the extent modified or otherwise indicated in the accompanying Opinion.

Other Findings of Fact and Conclusions of Law of the Commission are contained in the accompanying Opinion.

It is further ordered, That the following order to cease and desist be, and it hereby is, entered:

ORDER

I

It is ordered, That Jay Norris Corp., a corporation, its successors and assigns, and Joel Jacobs and Mortimer Williams individually and as officers of said corporation, and respondents' officers, agents, representatives and employees directly or through any corporation, subsidiary, division, trade style, or other device, in connection with the advertising, offering for sale, sale and distribution of general mail-order merchandise in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

1. Failing to refund the amount required by Paragraph 2, in connection with the return of merchandise purchased from respondents, within the time specified in respondents' advertisements. If no time is specified, such refund must be made within the time specified in Paragraph 5(E)(4) of this Part. [3]

2. Failing to refund the full purchase price of merchandise including postage, insurance, handling, shipping, or any other fee or charge paid by the purchaser any time a refund is made to such purchaser, unless respondents clearly state in their advertisement the exact nature of the refund including any items of the purchaser's expense that will not be refunded.

3. (A) Soliciting any order for the sale of merchandise to be ordered by the buyer through the mails unless, at the time of the solicitation, respondents have a reasonable basis to expect that they will be able to ship any ordered merchandise to the buyer: (1) within the time clearly and conspicuously stated in any such solicitation, or (2) if no time is clearly and conspicuously stated, within thirty (30) days after receipt of a properly completed order from the buyer; and

(B) Providing any buyer with any revised shipping date, as provided in Paragraph 4 of this Part unless, at the time any such revised shipping date is provided, respondents have a reasonable basis for making such representation regarding a definite revised shipping date; or

(C) Informing any buyer that they are unable to make any representation regarding the length of any delay unless (1) respondents have a reasonable basis for so informing the buyer and (2) respondents inform the buyer of the reason or reasons for the delay.

For purposes of this order, the failure of respondents to have records or other documentary proof establishing their use of systems and procedures which assure the shipment of merchandise in the ordinary course of business within any applicable time set forth in this order will create a rebuttable presumption that the respondents lacked a reasonable basis for any expectation of shipment within said applicable time. [4]

4. (A) Where respondents are unable to ship merchandise within the applicable time set forth in Paragraph 3(A) above, failing to offer to the buyer, clearly and conspicuously and without prior demand, an option either to consent to a delay in shipping or to cancel his order and receive a prompt refund. Said offer shall be made within a reasonable time after respondents first become aware of their inability to ship within the applicable time set forth in Paragraph 3(A), but in no event later than said applicable time.

(1) Any offer to the buyer of such an option shall fully inform the

buyer regarding his right to cancel the order and to obtain a prompt refund and shall provide a definite revised shipping date, but where respondents lack a reasonable basis for providing a definite revised shipping date the notice shall inform the buyer that respondents are unable to make any representation regarding the length of the delay.

(2) Where respondents have provided a definite revised shipping date which is thirty (30) days or less later than the applicable time set forth in Paragraph 3(A), the offer of said option shall expressly inform the buyer that, unless respondents receive, prior to shipment and prior to expiration of the definite revised shipping date, a response from the buyer rejecting the delay and cancelling the order, the buyer will be deemed to have consented to a delayed shipment on or before the definite revised shipping date.

(3) Where the respondents have provided a definite revised shipping date which is more than thirty (30) days later than the applicable time set forth in Paragraph 3(A), or where the respondents are unable to provide a definite revised shipping date and therefore inform the buyer that they are unable to make any representation regarding the length of the [5] delay, the offer of said option shall also expressly inform the buyer that his order will automatically be deemed to have been cancelled unless (a) respondents have shipped the merchandise within thirty (30) days of the applicable time set forth in Paragraph 3(A) above, and have received no cancellation prior to such shipment, or (b) respondents have received from the buyer within thirty (30) days of said applicable time, a response specifically consenting to said shipping delay. Where the respondents inform the buyer that they are unable to make any representation regarding the length of the delay, the buyer shall be expressly informed that, should he consent to an indefinite delay, he will have a continuing right to cancel his order at any time after the applicable time set forth in Paragraph 3(A) by so notifying respondents prior to actual shipment.

(4) Nothing in this paragraph shall prohibit respondents when they furnish a definite revised shipping date to Paragraph 4(A)(1) above, from requesting, simultaneously with or at any time subsequent to the offer of an option pursuant to Paragraph 4(A), the buyer's express consent to a further unanticipated delay beyond the definite revised shipping date. *Provided, however,* that where respondents solicit consent to an unanticipated indefinite delay the solicitation shall expressly inform the buyer that, should he so consent to an indefinite delay, he shall have a continuing right to cancel his order at any time after the definite revised shipping date by so notifying respondents prior to actual shipment.

(B) Where respondents are unable to ship merchandise on or before the definite revised shipping date provided under Paragraph 4(A)(1), and consented to by the buyer pursuant to Paragraphs 4(A)(2) and 4(A)(3), failing to offer to the buyer, clearly and conspicuously and without prior demand, a renewed option either to consent to a further [6] delay or to cancel the order and to receive a prompt refund. Said offer shall be made within a reasonable time after respondents first become aware of their inability to ship before the said definite revised date, but in no event later than the expiration of the definite revised shipping date. *Provided, however,* that where respondents previously have obtained the buyer's express consent to an unanticipated delay until a specific 4(A)(4) definite shipping date, pursuant to Paragraph 4 (A) (4) or to a further delay until a specific date beyond the definite revised shipping date pursuant to Paragraph 4(B), that date to which the buyer has expressly consented shall supersede the definite revised shipping date for purposes of Paragraph 4(B).

(1) Any offer to the buyer of said renewed option shall provide the buyer with a new definite revised shipping date, but where respondents lack a reasonable basis for providing a new definite revised shipping date, the notice shall inform the buyer that respondents are unable to make any representation regarding the length of the further delay.

(2) The offer of a renewed option shall expressly inform the buyer that, unless respondents receive, prior to the expiration of the old definite revised shipping date or any date superseding the old definite revised shipping date, notification from the buyer specifically consenting to the further delay, the buyer will be deemed to have rejected any further delay, and to have cancelled the order if respondents are in fact unable to ship prior to the expiration of the old definite revised shipping date or any date superseding the old definite revised shipping date. *Provided, however,* that where respondents offer the buyer the option to consent to an indefinite delay the offer shall expressly inform the buyer that, should he so consent to an indefinite delay, he shall have a continuing right to cancel his order at any time after the old definite revised shipping date or any date superseding the old definite revised shipping date. [7]

(3) Paragraph 4(B) shall not apply to any situation where respondents, pursuant to the provisions of Paragraph 4(A)(4), have previously obtained consent from the buyer to an indefinite extension beyond the first revised shipping date.

(C) Whenever a buyer has the right to exercise any option under this order or to cancel an order by so notifying respondents prior to shipment, failing to furnish the buyer with adequate means, at respondents' expense, to exercise such option or to notify respondents regarding cancellation. For the purposes of this order, the failure of respondents:

(1) To provide any offer, notice or action required by this order in writing and by first class mail will create a rebuttable presumption that the respondents failed to offer a clear and conspicuous offer, notice or option;

(2) To provide the buyer with the means in writing (by business reply mail or with postage prepaid by respondents) to exercise any option or to notify respondents regarding a decision to cancel, will create a rebuttable presumption that the respondents did not provide the buyer with adequate means pursuant to this Paragraph 4(C).

Nothing in Paragraph 4 of this Part shall prevent respondents where they are unable to make shipment within the time set forth in Paragraph 3(A) or within a delay period consented to by the buyer, from deciding to consider the order cancelled and providing the buyer with notice of said decision within a reasonable time after they become aware of said inability to ship, together with a prompt refund.

5. Failing to deem an order cancelled and to make a prompt refund to the buyer whenever:

(A) Respondents receive, prior to the time of shipment, notification from the buyer cancelling the order pursuant to any option, renewed option or continuing option under this order; [8]

(B) Respondents have pursuant to Paragraph 4(A)(3), provided the buyer with a definite revised shipping date which is more than thirty (30) days later than the applicable time set forth in Paragraph 3(A) or have notified the buyer that respondents are unable to make any representation regarding the length of the delay and respondents (1) have not shipped the merchandise within thirty (30) days of the applicable time set forth in Paragraph 3(A), and (2) have not received the buyer's express consent to said shipping delay within said thirty (30) days;

(C) Respondents are unable to ship within the applicable time set forth in Paragraph 4(B) and have not received, within the said applicable time, the buyer's consent to any further delay;

(D) Respondents have notified the buyer of their inability to make shipment and have indicated their decision not to ship the merchandise; or

(E) Respondents fail to offer the option prescribed in Paragraph

4(A) and have not shipped the merchandise within the applicable time set forth in Paragraph 3(A).

For purposes of this Part:

(1) "Shipment" shall mean the act by which the merchandise is physically placed in the possession of the carrier.

(2) "Receipt of a properly completed order" shall mean the time at which respondents receive an order from the buyer containing all the information requested by respondents and accompanied, where required, by the proper amount of money in the form of cash, check or money order. *Provided, however,* that where respondents receive notice that the check or money order tendered by the buyer has been dishonored or that the buyer does not qualify for a credit sale, "receipt of a properly completed order" shall mean the time at which (a) respondents receive notice that a check or money order for the proper amount tendered by the buyer has been honored, (b) the buyer tenders cash in the proper amount or (c) the seller receives notice that the buyer qualifies for a credit sale. [9]

(3) "Refund" shall mean:

(a) Where the buyer tendered full payment for the unshipped merchandise in the form of cash, check or money order, a return of the full amount tendered in the form of cash, check, or money order;

(b) Where there is a credit sale:

(i) and the seller is a creditor, a copy of a credit memorandum or the like or an account statement reflecting the removal or absence of any remaining charge incurred as a result of the sale from the buyer's account;

(ii) and a third party is the creditor, a copy of an appropriate credit memorandum or the like to the third party creditor which will remove the charge from the buyer's account or a statement from the seller acknowledging the cancellation of the order and representing that he has not taken any action regarding the order which will result in a charge to the buyer's account with the third party;

(iii) and the buyer tendered partial payment for the unshipped merchandise in the form of cash, check or money order, a return of the amount tendered in the form of cash, check or money order.

(4) "Prompt refund" shall mean:

(a) Where a refund is made pursuant to definition (3)(a) or (3)(b)(iii) a refund sent to the buyer by first class mail within seven (7) working days of the date on which the buyer's right to a refund vests under the provisions of this order.

(5) The "time of solicitation" of an order shall mean that time when respondents have:

(a) Mailed or otherwise disseminated solicitation to a prospective purchaser; [10]

(b) Made arrangements for an advertisement containing the solicitation to appear in a newspaper, magazine or the like or on radio or television which cannot be changed or cancelled without incurring substantial expense; or

(c) Made arrangements for the printing of a catalog, brochure or the like which cannot be changed without incurring substantial expense, in which the solicitation in question forms an insubstantial part.

6. Representing the safety or performance of any product unless such claims are fully and completely substantiated by a reasonable basis which shall consist of competent and objective material available in written form.

7. Misrepresenting that the nondelivery of merchandise ordered and paid for by a customer is caused by loss of the merchandise by the United States Postal Service.

8. Misrepresenting, directly or indirectly, the time or manner in which respondents' flame gun, or any other product used for the removal of snow or ice, will perform in the removal of snow or ice.

9. Misrepresenting, directly or indirectly, the time in which or the manner by which respondents' roach powder, or any other pesticide product, will kill or eliminate roaches.

10. Making any representation as to the safety of respondents' roach powder or other pesticide product without failing to clearly and conspicuously include the following statement in all advertisements and other promotional material for said products: "To use this product safely, you must follow the instructions on the label."

11. Misrepresenting, directly or indirectly, that respondents' TV antenna or any TV antennna will bring in sharp and clear reception and is superior to any other antenna. [11]

12. Making any representation as to the life expectancy of flashlights or other battery operated product without failing to disclose, clearly and conspicuously in all advertisements and other promotional material for such products (a) the expected "on" life of the product; and (b) any limitations on the warranty of such product.

13. Representing, directly or indirectly, that the Lincoln-Kennedy penny was minted by the United States Treasury Department.

14. Representing, directly or indirectly, that the Lincoln-Kennedy penny is a coin of historical and numismatic significance which is likely to increase in value.

15. Representing, directly or indirectly, in connection with the

sale of any product that another product is given "free" or as a gift without cost or charge in connection with:

a. any offer which runs for an indefinite term or continuously for a period in excess of one (1) year; or

b. any offer not covered by (a) above, excluding introductory offers, unless as to such limited offer:

(1) a regular bona fide retail price is established for the product without the "free" product;

(2) a regular bona fide retail price is established for the "free" product, or in the absence of such price a determination is made of the cost to respondents of such other product; and

(3) the price of the product is reduced at least as much as the price or cost of the "free" product. [12]

II

It is further ordered, That Jay Norris Corp., and Pan-Am Car Distributors Corp., corporations, their successors and assigns, and Joel Jacobs, Mortimer Williams and Kenneth Mann, individually and as officers of said corporations, and respondents' officers, agents, representatives and employees directly or through any corporation, subsidiary, division, trade style, or other device, in connection with the advertising, offering for sale, sale and distribution of used motor vehicles by mail-order in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

1. Misrepresenting, directly or by implication, the ease or profit with which purchasers can resell respondents' motor vehicles;
2. Misrepresentating the mechanical and physical condition of said motor vehicles;
3. Misrepresenting that said motor vehicles are in safe mechanical and operating condition;
4. Misrepresenting the extent to which said motor vehicles have been inspected and repaired in preparation for sale and delivery to customers;
5. Misrepresenting that said motor vehicles are in sound condition and repair and will render normal, adequate and satisfactory service; and
6. Representing the safety or performance of said motor vehicles unless such claims are fully and completely substantiated by a reasonable basis which shall consist of competent and objective material available in written form.

III

It is further ordered, That:

1. Respondents shall maintain records of all consumer complaints for a period of three years after such complaint is received, including, but not limited to the following information: [13]

a. Name and address of the consumer;
b. Date of receipt of the complaint;
c. Transaction about which complaint is received;
d. Nature of the complaint; and
e. Date and disposition of the complaint.

2. Respondents shall notify the Commission at least thirty (30) days prior to any proposed changes in the corporate respondents such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other changes in the corporation which may affect compliance obligations arising out of the order.

3. The individual respondents named herein, shall promptly notify the Commission of the discontinuance of their present business or employment and of their affiliation with a new business or employment. Such notice shall include respondents' current business address and a statement as to the nature of the business or employment in which they are engaged as well as a description of their duties and responsibilities.

4. Respondents shall deliver a copy of this order to cease and desist to all personnel or agents of respondents responsible for the preparation, creation, production or publication of the advertising of all products covered by this order.

5. No provision of this order shall be construed in any way to annul, invalidate, repeal, terminate, modify or exempt respondents from complying with agreements, orders or directives of any kind obtained by any other agency or act as a defense to actions instituted by municipal or state regulatory agencies. No provision of this order shall be construed to imply that any past or future conduct of respondents complies with the rules and regulations of, or the statutes administered by the Federal Trade Commission. [14]

6. Respondents herein shall, within sixty (60) days after service of this order, and annually for five (5) years thereafter, file with the Commission a written report setting forth in detail the manner and form of their compliance with this order. The expiration of the obligation to file such reports shall not affect any other obligation arising under this order.

IV

It is further ordered, That the allegations of the complaint are dismissed as to FEDERATED NATIONWIDE WHOLESALERS SERVICE, GARYDEAN CORP., t/a Nationwide Wholesalers Service, and P-N PUBLISHING COMPANY, INC.

IN THE MATTER OF

PERFORMANCE SAILCRAFT INC.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SECTION 5 OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2922. Complaint, May 2, 1978 —Decision, May 2, 1978

Consent order requiring a Pointe-Claire, Quebec, Canada, manufacturer and distributor of fiberglass sailboats and accessories, among other things, to cease entering into or enforcing any form of agreement with its dealers concerning the retail price of its products; restricting territories in which its dealers may advertise or sell its products; and terminating or threatening to terminate dealers who do not follow its pricing and territorial instructions. Further, any future price lists distributed by the firm must note that the prices are suggested or approximate.

Appearances

For the Commission: *Allen R. Caskie.*

For the respondent: *R. Warden McKimm,* Ottawa, Canada.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, as amended, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Performance Sailcraft Inc., a corporation, more particularly described and referred to hereinafter as respondent, has violated the provisions of Section 5 of the Federal Trade Commission Act (38 Stat. 719, as amended; 15 U.S.C. 45), and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges with respect thereto as follows:

PARAGRAPH 1. Respondent Performance Sailcraft Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the province of Quebec, Canada, with its principal office and place of business at 91 Hymus Boulevard, Pointe-Claire, Quebec, Canada.

PAR. 2. Respondent is a manufacturer and distributor of small recreational sailboats of fiberglass construction and accessories to be used therewith.

In 1975, respondent's gross income from sales of said products was $3.6 million, over $2 million of which was derived from sales in the United States.

PAR. 3. In the course of conduct of its business of manufacturing and distributing sailboats and accessories, respondent is engaged in transacting business within the United States through the following activities, among others: the placement of advertising in United States magazines and newspapers of interstate circulation; the presence within the United States and participation of respondent's salesmen at numerous trade shows; and the C.O.D. shipment of respondent's products from its principal place of business to independent dealers located in various States throughout the United States who sell the products to consumers.

There is now and has been for several years past, a constant, substantial and increasing flow of such products in or affecting "commerce" as that term is defined in the Federal Trade Commission Act, as amended.

PAR. 4. In the course and conduct of its business in or affecting commerce, except to the extent that competition has been hampered or restrained by reason of the practices hereinafter alleged, respondent has been and is now in competition with other persons, firms and corporations engaged in the manufacture, sale and distribution of said products.

PAR. 5. Respondent, in combination, agreement, or understanding with certain of its authorized dealers, or with the cooperation or acquiescence of other of its dealers, has for the last several years been engaged in a planned course of action to fix, establish and maintain certain resale or retail prices at which said products are resold. In furtherance of said planned course of action, respondent has for the past several years engaged in the following acts or practices, among others:

(a) Regularly furnishing its dealers with price lists and necessary supplements thereto containing certain resale or retail prices;

(b) Establishing agreements, understandings, or arrangements with its dealers, as a condition precedent to the granting of a dealership, that such dealers will maintain certain resale or retail prices;

(c) Informing its dealers, by direct or indirect means, that respondents expect and require such dealers to maintain and enforce certain resale or retail prices or such dealerships will be terminated;

(d) Soliciting and obtaining from its dealers cooperation and assistance in identifying and reporting any dealer who advertises, or offers to sell, or sells said products at prices lower than certain resale or retail prices.

PAR. 6. Respondent, in combination, agreement, or understanding with certain of its authorized dealers, or with the cooperation or acquiesence of other of its dealers, has for the last several years been engaged in a planned course of action whose effect has been to foster, promote, maintain and support its policies of restricting dealer competition in the United States in the marketing, sale, and distribution of fiberglass sailboats by directing, encouraging, threatening, warning, and/or otherwise prohibiting its dealers from selling or advertising the sale of said products outside of their allocated territories.

PAR. 7. These aforesaid acts and practices as alleged, are prejudicial and injurious to the public; have a tendency to hinder, restrict, restrain and prevent competition and have actually hindered, restricted, restrained and prevented competition; and constitute unfair acts or practices and unfair methods of competition in or affecting commerce within the meaning and intent of Section 5 of the Federal Trade Commission Act, as amended.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Washington, D.C. Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act, as amended; and

The respondent and its counsel and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent Performance Sailcraft Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the province of Quebec, Canada, with its principal office and

place of business at 91 Hymus Boulevard, Pointe-Clare, Quebec, Canada.

2. The Federal Trade Commission has jurisdiction of the subject matter of the proceeding and the respondent, and the proceeding is in the public interest.

ORDER

I. *It is ordered,* That respondent Performance Sailcraft Inc., and its subsidiaries, divisions, licensees, successors, assigns, officers, directors, agents, representatives and employees, directly or indirectly, or through any corporate or other device, in connection with the distribution, advertising, offering for sale, or sale of fiberglass sailboats and accessories, or any other products (hereinafter referred to in this order as "said products"), in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, as amended, shall forthwith cease and desist from:

A. Establishing, maintaining or enforcing any contract, agreement, understanding or arrangement fixing, establishing, maintaining, controlling, influencing or enforcing in any way or to any extent, directly or indirectly, the price at which any of said products is advertised, sold or offered for sale at retail.

B. Requiring any dealer or prospective dealer to enter into any oral or written agreement or understanding that such dealer or prospective dealer will maintain any resale or retail price for any of said products as a condition of buying any of said products.

C. Requesting or requiring any dealer or prospective dealer, either directly or indirectly, to report any dealer, person or firm who does not adhere to any resale or retail price for any of said products, or acting on reports so obtained by refusing or threatening to refuse sales to any dealer, person or firm so reported.

D. Threatening to terminate or terminating, either directly or indirectly, any dealer for failure to observe, maintain or advertise respondent's suggested resale prices for said products.

E. Requiring, from any dealer charged with price cutting or failure to adhere to any resale or retail price, a promise or assurance to adhere to any resale or retail price for any of said products as a condition precedent to any future sales to said dealer.

F. Publishing, disseminating or circulating any price list, price book, price tag, advertising or promotional material, or other document indicating any resale or retail price without stating on each page (of such list, book, tag, advertising or promotional material or other document), on which a price appears, that the price is suggested or approximate.

G. Imposing or attempting to impose any limitations or restrictions respecting the territories in which said products may be advertised or sold by its dealers.

H. Attempting to enter into, entering into, continuing, maintaining, or enforcing any contract, combination, understanding or agreement to limit, allocate, or restrict the territory in which said products may be advertised or sold by its dealers.

I. Requesting or requiring any dealer or prospective dealer, either directly or indirectly, to report any dealer, person or firm who does not adhere to any territorial restriction in the advertising and sale of any of said products, or acting on reports so obtained by refusing or threatening to refuse sales to any dealer, person or firm so reported.

J. Threatening to terminate or terminating, either directly or indirectly, any dealer for failure to limit or restrict the advertising and sale of said products to a specified territory.

Providèd, that none of the provisions herein shall prohibit respondent from designating geographical areas within which a dealer may agree to devote his best efforts to the sale of said products (hereinafter "area of primary responsibility") as a condition of becoming a dealer or maintaining a dealership, provided that such dealers are told that said area is not exclusive and does not place a territorial restriction upon the sale of said products.

Provided further, that none of the provisions herein shall prohibit respondent from terminating dealers for lawful business reasons.

II. *It is further ordered,* That the respondent shall within sixty (60) days after the service upon it of this order, mail a copy of this order to each of its dealers of said products in the United States and, during the five (5) year period of time following the date of service of this order, to all of its future dealers in the United States at the time said dealers are opened as accounts, under cover of the letter annexed hereto as Exhibit A, and furnish the Commission proof of the mailing thereof in the file required to be maintained under Paragraph V herein.

III. *It is further ordered,* That respondent shall forthwith distribute a copy of this order to each of its operating divisions engaged in the manufacture, sale, marketing and distribution of said products and to all of its sales personnel connected with the sale, marketing, and distribution of said products and shall instruct each sales person employed by it now or in the future to read this order and to be familiar with its provisions.

IV. *It is further ordered,* That respondent notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation of or dissolution of subsidiaries or any other such change in the corporation which may affect compliance obligations arising out of the order.

V. *It is further ordered,* That the respondent herein, for a period of five (5) years from the date of this signing, establish and maintain a file of all records referring or relating to respondent's refusal to sell said products to any of respondent's dealers, which file shall contain the names and addresses of all dealers with whom respondent has refused to deal since the effective date of the order, a description of the reason for the refusal, the date of the refusal, and a record of a communication to each such dealer explaining respondent's refusal to sell said products, and which file will be made available on reasonable notice for inspection at the Commission's offices in Washington, D.C.

VI. *It is further ordered,* That the respondent herein shall within sixty (60) days after service upon it of this order file with the Commission a report, in writing, setting forth in detail the manner and form in which it has complied with this order.

EXHIBIT A

(Letterhead of Performance Sailcraft Inc.)

Dear Dealer:

PSI has entered into an agreement with the Federal Trade Commission relating to our territorial allocation and pricing policies. A copy of the consent order entered into pursuant to that agreement is enclosed herewith.

We have entered into this agreement solely for the purpose of settling a dispute with the Commission, and the agreement and consent order are not to be construed as an admission that we have violated any of the laws administered by the Commission, or that any of the allegations in the complaint are true and correct. Instead, the order merely relates to our activities in the future.

In order that you may readily understand the terms of the consent order, we have set forth the essentials of the agreement with the Commission, although you must realize that the consent order itself is controlling rather than the following explanation of its provisions:

(1) Our dealers are free to set their own retail or resale prices for the products covered by the consent order.

(2) We will not solicit, invite or encourage any dealer or any other person to report any dealer not following any retail or resale price for any of said products, and, furthermore, will not act on any such report sent to us.

(3) We will not require or induce our dealers to refrain from advertising said products at any price or from selling or offering said products at any price to any person.

(4) As you know, it is a condition of becoming a dealer or maintaining a dealership that you agree to devote your best sales efforts in your designated geographical territory. However, you are free to advertise and sell any of the products covered by the consent order outside of these designated territories.

Sincerely,
(Officer)

IN THE MATTER OF

CHRYSLER CORPORATION, ET AL.

Docket 9072. Interlocutory Order, May 8, 1978

Denial of complaint counsel's motion to enforce subpoena *duces tecum* against present owner of records sought, a purchaser of the assets of the corporation named in the subpoena.

ORDER DENYING MOTION TO ENFORCE SUBPOENA DUCES TECUM

On February 13, 1978, Administrative Law Judge Lewis F. Parker certified to the Commission the motion of complaint counsel herein for enforcement of a subpoena *duces tecum* issued in November, 1976,[1] directing Northline Dodge, Inc., a California corporation, to produce certain documents relating, *inter alia*, to motor vehicle repossessions in which it had been involved during a specified time period. A partial return was made, and complaint counsel were pursuing further compliance when, on July 29, 1977, complaint counsel were advised that the assets of the California corporation had been sold to a Texas corporation having different principals but the same name, and the California corporation dissolved. The assets transferred evidently include the records sought, to the extent they exist, but complaint counsel assert that the Texas corporation has declined to take the effort necessary to make any further return on the subpoena. Matters were in this posture when complaint counsel moved for enforcement of the subpoena.

Complaint counsel's motion does not attempt to propound a theory for enforcing a subpoena *duces tecum* against a corporation which simply purchased assets from the corporation against which it was issued. It is patent, however, that mere identity of name between the two corporations has no bearing on the matter. The subpoena was issued against and served upon a particular legal entity. While that legal entity retains the capacity to be sued for some period of time after formal dissolution, it evidently no longer possesses the documents sought. The legal entity which does possess the documents, on the other hand, has never been subpoenaed to produce them. Moreover, there is nothing in the record to indicate that the new entity stands in the position of a legal successor to the dissolved corporation so as to enable the outstanding subpoena to be enforced against the Texas corporation. In these circumstances, an order that the November 1976 subpoena be enforced would appear to be an exercise in futility. Accordingly,

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[1] The exact date does not appear from the materials before us. Indeed, as complaint counsel note, the copy of the subpoena attached to the motion herein does not show on its face that it was authorized by the ALJ. Because of our disposition of the matter we need not consider the effect, if any, of this omission. The ALJ has, of course, stated that he issued the subpoena.

It is ordered, That complaint counsel's Motion to Enforce Subpoena *Duces Tecum* be, and it hereby is, denied.[3]

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[3] This ruling, of course, in no way precludes complaint counsel from seeking to subpoena the documents directly from the new corporation.

IN THE MATTER OF

AMERICAN DENTAL ASSOCIATION, ET AL.

Docket 9093. Interlocutory Order, May 8, 1978

Denial of supplemental motions of subpoenaed third parties to quash and/or limit subpoenas *duces tecum*.

ORDER DENYING MOTION TO QUASH AND/OR LIMIT SUBPOENAS DUCES TECUM

This matter comes to the Commission upon supplemental motions to quash and/or limit subpoenas *duces tecum* filed on behalf of Henry L. Ernstthal and the California Dental Association ("CDA") and Kathie Boise and the Orange County Dental Society, Inc. ("OCDS"). Because of the unusual posture of this motion, it is necessary to chronicle the prior developments in some detail.

The Commission issued an administrative complaint in this proceeding on January 4, 1977. In the course of the administrative proceedings, the administrative law judge ("ALJ"), at the request of Commission complaint counsel, on November 16, 1977, issued subpoenas *duces tecum* to CDA and OCDS pursuant to Section 3.34(b) of the Commission's Rules of Practice and Procedures. CDA and OCDS filed a joint motion to quash the subpoenas on December 1, 1977, which motion was denied by the ALJ on December 15, 1977. CDA and OCDS then filed a joint motion on January 3, 1978, seeking extraordinary leave to appeal to the Commission the denial of their motion to quash. On January 6, 1978, this motion was denied by the ALJ, who established January 23, 1978, as the final date for compliance with the subpoenas. CDA and OCDS moved before the ALJ on January 18, 1978, for reconsideration of his denial of their motion to quash and their motion for appeal to the Commission, arguing for the first time that the Commission lacked jurisdiction over the parties. The ALJ denied this motion on January 23, 1978. Upon the parties' subsequent refusal to comply with the subpoenas, on February 17, 1978, the Commission granted complaint counsel's motion requesting court enforcement of the subpoenas and enforcement papers were filed on March 14, 1978.

In an order issued April 19, 1978, the District Court for the District of Columbia concluded that it was inappropriate to consider the parties' jurisdictional challenge to the Commission's pending adjudicative proceeding. However, the court found that the ALJ had not had an opportunity to consider some of the parties' non-jurisdictional challenges. Accordingly, the court's order permits respondents to present to the ALJ by April 21, 1978, any of the non-jurisdictional challenges which they raised in the enforcement proceedings but which were not initially presented to the ALJ. The court's order further provides that the ALJ shall rule on any such challenges no later than April 28, 1978, and that after the ALJ has so ruled (and the Commission, if requested, has reviewed the matter), CDA and OCDS may assert in the enforcement proceeding any non-jurisdictional challenges to the instant subpoenas *duces tecum*. The order specifically indicates that the court will retain jurisdiction over the Commission's present enforcement petition pending the ALJ's consideration (and the Commission's, if so requested) of non-jurisdictional challenges not previously presented by the parties to the ALJ.

Pursuant to this order, CDA and OCDS filed the instant supplemental motion to quash and/or limit the subpoenas *duces tecum* on April 21, 1978, arguing that the specifications of the subpoenas are overly broad, seek irrelevant information, and are too indefinite. Additionally, the parties contend that compliance with the subpoenas would be unduly burdensome and that they are entitled to a protective order for confidential documents. By orders of April 28, May 1, and May 2, 1978, the ALJ issued a protective order but otherwise denied the supplemental motion and certified the matter to the Commission for its consideration in view of the order of the district court.[1]

Ordinarily, under the Commission's Rules of Practice and Procedure the supplemental motion would have been untimely since no good cause for a belated, piecemeal submission has been shown to justify an extension under Section 3.34(b). Moreover, even had it been timely, the ALJ's denial of that motion, like other pre-trial discovery rulings, would not be reviewed by the Commission absent a showing (not made here) of a clear abuse of discretion. *See, e.g., Exxon Corp.*, 85 F.T.C. 91 (1975). The opposition of CDA and OCDS to court enforcement of the subpoena did not focus on a supplemental motion to quash as a form of relief, and the status of such motion under the Commission's Rules was not addressed in the litigation papers. Accordingly, the court had no reason to know that the review apparently contemplated by the court's order would ordinarily be unavailable, and it is open to question whether the court intended to require the Commission to engage in extraordinary review in this matter.

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[1] We understand that the May 31, 1978 compliance date established by the ALJ is contingent upon the district court's enforcement of the subpoenas.

Nevertheless, in a spirit of compliance with the court's order and to forestall further delay in enforcement of the subpoenas,[2] the Commission has reviewed the ALJ's denial of the supplemental motion. Our review convinces us that there is no showing sufficient to warrant reversal of the ALJ's well-considered ruling. Accordingly,

It is ordered, That the Supplemental Motion to Quash and/or Limit the Subpoenas *Duces Tecum* is denied.

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[2] We assume that the court did not intend to endorse any generally-applicable departure from the usual principle requiring exhaustion of administrative remedies, under which legal or factual arguments not tendered in a timely motion to quash a subpoena would be deemed waived.

In the Matter of

GEORGIA-PACIFIC CORPORATION

MODIFYING ORDER IN REGARD TO ALLEGED VIOLATIONS OF THE FEDERAL TRADE COMMISSION AND SEC. 7 OF THE CLAYTON ACTS

Docket 8843. Final Order, Dec. 26, 1972—Modifying Order, May 12, 1978

This order modifies a final order to cease and desist issued December 26, 1972, 38 FR 1581, 81 F.T.C. 984, by changing Paragraphs 6 and 7 to permit acquisitions of $1,000,000 or less without prior Commission approval, and by substituting for Paragraph 10, one that limits reporting obligations to those corporate alterations that may have a significant affect on compliance.

Order Modifying Order to Cease and Desist

By a petition filed March 31, 1978, and revised by a petition filed April 26, 1978, respondent Georgia-Pacific Corporation asked the Commission to reopen this proceeding to modify Paragraphs 6, 7, and 10 of the consent order issued by the Commission on December 26, 1972.

Paragraph 7 of the consent order requires, *inter alia,* that Georgia-Pacific obtain Commission approval before purchasing non-softwood plywood assets when the seller is engaged in softwood plywood manufacturing. Georgia-Pacific contends that this reporting requirement is overbroad because the consent order was aimed at preventing Georgia-Pacific from increasing its market power in the softwood plywood industry, and it is unlikely that its ability to control price or entry in the relevant market would be affected when the acquisition is of non-softwood plywood assets.

Respondent also requests modification of Paragraphs 6 and 7 of the order so that it need not obtain approval of acquisitions of softwood plywood assets where the purchase price is less than 1 million dollars. Respondent believes that purchases of this size are *de minimis* and "would not undercut the effectiveness of the consent order, but it would reduce needless administrative burdens arising from compliance with the consent order. . . ." More precisely, respondent contends that it is unable to bid at auctions for softwood plywood equipment owned by softwood plywood firms, as these auctions often take place upon relatively short notice which precludes the soliciting and receiving of prior approval from the Commission. Because of their *de minimis* nature, these asset acquisitions, respondent believes, would likely be approved by the Commission.

The final modification sought by Georgia-Pacific relates to Paragraph 10 of the consent order. This paragraph requires respondent to notify the Commission of the creation or dissolution of subsidiaries even if the corporate change does not affect compliance obligations arising from the order. Respondent is a large, multinational corporation which periodically must, it represents, "make various adjustments in its corporate structure which do not or would not affect its compliance obligations." The modification proposed by respondent will limit its reporting obligations under Paragraph 10 to those corporate alterations that may have significance from a compliance standpoint.

The Bureau of Competition filed on May 1, 1978, an answer to respondent's petition. The Bureau does not oppose the modifications.

We agree that the petition should be granted. The modifications proposed by respondent should not affect adversely the purpose of the order, which, is to say, the aspects of the order complained of by respondent are either unnecessary or overbroad, and they are, therefore, unwarranted.

Accordingly,

It is ordered, That the proceeding be, and it hereby is, reopened.

It is further ordered, That the order to cease and desist be, and it hereby is, modified by substituting for Paragraphs 6, 7 and 10 of the order, the following:

PARAGRAPH 6

It is further ordered, That for ten (10) years from the effective date, respondent shall cease and desist from acquiring, directly or indirectly through subsidiaries, or otherwise, for its use in the manufacture of softwood plywood, from any person, firm or corporation other than the manufacturer thereof or a regular dealer or distributor of such equipment in the ordinary course of such dealer's or distributor's business:

(A) Any equipment specifically designed for the manufacture of softwood plywood;

(B) Any equipment specifically designed and theretofore used in the manufacture of softwood plywood; and

(C) Any equipment thereafter converted by respondent, directly or indirectly, into equipment specifically designed for the manufacture of softwood plywood; unless such acquisitions amount to $1,000,000 or less from any one person, firm or corporation in any twelve month period in the absence of prior Federal Trade Commission approval of such acquisition.

PARAGRAPH 7

It is further ordered, That for a period of ten (10) years from the effective date, respondent shall cease and desist from acquiring, directly or indirectly, through subsidiaries, or otherwise, the whole or any part of the share capital or assets of, or any other interest in, any other person, firm or corporation engaged in the manufacture of softwood plywood in the United States immediately prior to such acquisition, unless such asset acquisitions amount to $1,000,000 or less from any one person, firm or corporation in any twelve-month period, in the absence of prior Federal Trade Commission approval of such acquisition; *Provided, however,* That nothing contained in this paragraph shall preclude or be deemed to preclude respondent from acquiring timberlands or any interest therein or timber in any form (including but not limited to stumpage, logs, veneers, chips, sawdust and cores); and, *Further provided,* That nothing contained in this paragraph shall apply to purchases of lumber, plywood, machinery, or any other product, by respondent in the regular conduct of its business from suppliers in the regular conduct of their businesses, or to sales made by respondent in the regular conduct of its business.

PARAGRAPH 10

It is further ordered, That for a period of ten (10) years from the effective date of the order entered by the Commission on December 26, 1972, respondent shall notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent which may affect compliance obligations arising out of the order, such as dissolution, assignment or sale resulting in the emergence of a successor corporation, or the creation or dissolution of subsidiaries or joint ventures.

IN THE MATTER OF

BELTONE ELECTRONICS CORPORATION, ET AL.

Docket 8928. Interlocutory Order, May 12, 1978

Remand for additional hearings ordered for consideration of customer and territorial restriction on interbrand and intrabrand competition.

ORDER REMANDING FOR ADDITIONAL HEARINGS

By order of July 5, 1977, the Commission directed the parties in this proceeding to submit supplemental briefs concerning the impact of *Continental T.V., Inc.* v. *GTE Sylvania, Inc.*, 433 U.S. 36 (1977). After careful review of the briefs submitted by the parties and the record developed before the administrative law judge ("ALJ"), the Commission has determined that a limited remand of the case is necessary for consideration of the impact of respondents' customer and territorial restrictions upon both interbrand and intrabrand competition.

The complaint in this proceeding was issued on May 8, 1973, charging respondents with various violations of Section 5, including, *inter alia,* imposition of exclusive dealing, maintenance of territorial and customer restrictions, use of certain post-termination restraints, and misappropriation of the names and addresses of dealers' customers. After extensive pretrial discovery and 115 days of hearings in Washington, D.C., Chicago, San Francisco, and New Orleans, the ALJ filed his initial decision on September 7, 1976, finding that the respondents had engaged in the following unfair acts and practices and unfair methods of competition in violation of Section 5:

(A) Requiring their selected dealers to sell Beltone products within assigned geographic territories;

(B) Requiring their selected dealers to deal exclusively in Beltone hearing aids:

(C) Prohibiting their dealers from dealing with certain potential customers;

(D) Preventing others, not their dealers, from dealing in or repairing Beltone products; and

(E) Appropriating and using for their own purposes the names and addresses of their dealers' customers.

The ALJ's legal analysis of respondents' territorial and customer restrictions (ID 79-82)[1] leaves no doubt that he examined these particular restraints in light of the then-prevailing *per se* standard of *United States* v. *Arnold, Schwinn & Co.*, 388 U.S. 365 (1967), under the rationale that conduct violating the Sherman Act would necessarily violate Section 5 of the FTC Act. Moreover, complaint counsel's trial and answering briefs indicate that they contemplated application of a *per se* theory throughout the proceeding. Although the record contains some discussion of the competition effects of respondents' territorial and customer restrictions, it is clear that the evidence introduced provides, on balance, an incomplete picture of the interbrand and intrabrand effects of these practices. Hence, the need to premise our disposition of this case upon a thorough examination of the competitive impact of these specific restraints leads us to conclude that we should remand the proceeding.[3] Accordingly,

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[1] We recognize, of course, that respondents deny the existence of any territorial or customer restrictions and we reach no final determination now on this issue or the other issues raised in the complaint.

It is ordered, That this matter is remanded to the administrative law judge for an expedited proceeding solely to receive additional evidence regarding the effects of respondents' territorial and customer restrictions upon interbrand and intrabrand competition.

It is further ordered, That, after the receipt of such additional evidence, the administrative law judge certify the record to the Commission together with any findings of fact or conclusions of law which he may make in light of the additional evidence.

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[3] In view of the unusual amount of cumulative dealer testimony evident in the present record, we wish to emphasize that an expeditious resolution of the issues on remand is in the best interest of all parties. To this end, stipulations should be freely utilized to avoid the introduction of duplicative testimony. In any event, we assume that the ALJ will exercise appropriate control over the receipt of additional evidence.

In the Matter of

SUNKIST GROWERS, INC.

Docket 9100. Interlocutory Order, May 15, 1978

Application for review of ALJ order denied for failure to raise an issue having substantial ground for difference of opinion.

Order Denying Application for Review

Respondent, Sunkist Growers Inc. ("Sunkist"), has filed an Application for Review of Order Denying Respondent's Motion to Dismiss for Lack of Jurisdiction pursuant to Rule 3.23(b). Because Sunkist has failed to raise an issue as to which there is substantial ground for difference of opinion, the Application for Review is denied. While further elaboration is unnecessary, a brief explanation of the reasons for our decision seems warranted.

Sunkist argues that the Commission lacks jurisdiction over the subject matter of this proceeding by reason of the Capper-Volstead Act, 7 U.S.C. 291, 292. Alternatively, Sunkist argues that primary jurisdiction of this matter rests with the Secretary of Agriculture.

It is well settled that the Capper-Volstead Act does not vest exclusive jurisdiction of antitrust claims against agricultural cooperatives in the Secretary of Agriculture. *Maryland & Virginia Milk Producers Ass'n, Inc.* v. *United States*, 362 U.S. 458, 462–64 (1960); *United States* v. *Borden Co.*, 308 U.S. 188, 205–06 (1939); *Central California Lettuce Producers Cooperative*, Dkt. 8970, slip opinion at 4–5 (July 25, 1977) [90 F.T.C. at 53,54], Cf. *Washington Crab Ass'n*, 66 F.T.C. 45 (1964). While conceding that federal courts have jurisdiction over monopolization suits initiated by the Department of Justice, Sunkist argues that the Commission lacks similar jurisdiction with respect to complaints issued under the Federal Trade Commission Act. Respondent, however, cites no authority in support of this anomalous position. The complaint alleges that Sunkist is a corporation within the meaning of Section 4 of the Federal Trade Commission Act which has engaged in unfair methods of competition. It thus appears that the complaint states a cause of action under Section 5 against a respondent which is subject to the Commission's jurisdiction.

Respondent's alternative argument is that "primary jurisdiction rests with the Secretary of Agriculture." As we explained in *Perpetual Federal Savings & Loan Ass'n*, Dkt. 9083 (December 6, 1977) [90 F.T.C. 608], it is not wholly clear that the doctrine of primary jurisdiction, which requires a court to defer the exercise of its jurisdiction until an administrative agency has determined a particular question, applies as between agencies. *Id.*, slip opinion at 24 n. 28 [90 F.T.C. at 662]. Assuming, *arguendo*, the applicability of the doctrine, it appears that the tests of *Ricci* v. *Chicago Mercantile Exchange*, 409 U.S. 289 (1973), are not met. The cases cited above indicate that the provisions of the Capper-Volstead Act are not incompatible with the maintenance of this action. Moreover, the Capper-Volstead Act gives the Secretary of Agriculture authority to adjudicate whether a cooperative association "monopolizes or restrains trade . . . to such an extent that the price of any agricultural product is unduly enhanced thereby." On the other hand, a monopolization complaint[1] under Section 2 of the Sherman Act or Section 5 of the Federal Trade Commission Act involves only an inquiry into whether monopoly power exists, and whether that monopoly power has been willfully acquired or maintained, *United States* v. *Grinnell Corp.*, 384 U.S. 563, 570–71 (1966), without any necessary showing of price enhancement. For this reason, it does not appear that facets of this dispute are necessarily within the jurisdiction of the Secretary of Agriculture, nor that adjudication by the Secretary would be of material aid in resolving the issues posed by the complaint. With respect to the latter point, it is clear that an adjudication by the Secretary that respondent had not unduly enhanced prices would in no way dispose of, or shed much significant light on, the issues in this case. Thus, it does not appear that the doctrine of primary jurisdiction requires us to defer to the Secretary of Agriculture. Accordingly,

It is ordered, That Respondent's Application for Review be, and the same hereby is, denied.

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[1] We note that while the gravamen of the complaint is monopolization, other charges, including violations of Section 7 of the Clayton Act, are encompassed within the complaint.

IN THE MATTER OF

VERRAZZANO TRADING CORPORATION, ET AL.

ORDER, OPINION, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION, WOOL PRODUCTS LABELING AND TEXTILE FIBER PRODUCTS IDENTIFICATION ACTS

Docket 9038. Complaint, June 24, 1975 — Final Order, May 15, 1978

This order, among other things, requires a New York City importer and distributor of wool and textile fiber products, and four affiliated companies, to cease misrepresenting or failing to properly disclose the fiber content of wool and textile fiber products, and the residual shrinkage of such products. Additionally, the firms must file bond with the Secretary of the Treasury before participating in the importation of wool and textile fiber fabrics; and provide purchasers of mislabeled merchandise with a copy of the order.

Appearances

For the Commission: *Ellen Zweibel* and *Judith K. Braun.*

For the respondents: *David A. Botwinik, Pavia & Harcourt,* New York City.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, the Wool Products Labeling Act of 1939 and the Textile Fiber Products Identification Act, and by virtue of the authority vested in it by said Acts, the Federal Trade Commission, having reason to believe that Verrazzano Trading Corporation, a corporation, Francisco Datini Inc., a corporation, Lanificio Tuscania Inc., a corporation, Lima Textiles Inc., a corporation, and Walter Banci, individually and as an agent for said corporations and as an officer of Lanificio Tuscania Inc. and Lima Textiles Inc. and as a partner trading and doing business as Lanificio Walter Banci s.a.s., hereinafter referred to as respondents, have violated the provisions of said Acts and the rules and regulations promulgated [2] under the Wool Products Labeling Act of 1939 and the Textile Fiber Products Identification Act, and it now appearing to the Commission that a proceeding by it in respect thereto would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent Verrazzano Trading Corporation is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York, with its main office and principal place of business at 2 Penn Plaza, New York, New York.

Respondent Francesco Datini Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York, with its main office and principal place of business at 2 Penn Plaza, New York, New York.

Respondent Lanificio Tuscania Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York with its main office and principal place of business at 2 Penn Plaza, New York, New York.

Respondent Lima Textiles Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York, with its main office and principal place of business at 2 Penn Plaza, New York, New York.

Individual respondent Walter Banci is an agent of said corporations and an officer of Lanificio Tuscania Inc. and Lima Textiles Inc. and a partner trading and doing business as Lanificio Walter Banci s.a.s. Lola Conti Banci is a co-partner but is inactive with respect to the business operations of said company. Walter Banci formulates, directs and [3] controls the acts and practices of said partnership and of said corporate respondents, including the acts and practices hereinafter set forth. His business address is the same as that of the corporate respondents.

The corporate respondents and Walter Banci constitute a unified family business operation designed to import and sell in the United States fabrics produced and exported from Italy by Lanificio Walter Banci, s.a.s. and distribute such fabrics in commerce.

PAR. 2. Respondents are now and for some time past have been engaged in the introduction, sale, advertising, and offering for sale, in commerce, and in the transportation or causing to be transported in commerce, and in the importation into the United States, of textile fiber products; and have sold, offered for sale, advertised, delivered, transported and caused to be transported, textile fiber products which have been advertised or offered for sale in commerce, and have sold, offered for sale, advertised, delivered, transported, and caused to be transported after shipment in commerce, textile fiber products as the terms "commerce" and "textile fiber product" are defined in the Textile Fiber Products Identification Act.

PAR. 3. Certain of said textile fiber products were misbranded by respondents within the intent and meaning of Section 4(a) of the Textile Fiber Products Identification Act and the rules and regulations promulgated thereunder, in that they were falsely and deceptively stamped, tagged, labeled, invoiced, advertised or otherwise identified as to the name or amount of the constituent fibers contained therein.

Among such misbranded textile fiber products, but not limited thereto, were certain textile fabrics stamped, tagged, labeled or otherwise identified by respondents as "50% cotton, 35% polyester, 15% nylon" whereas, in truth and in fact, said products contained substantially different fibers and amounts of fibers than represented. [4]

PAR. 4. Certain of such textile fiber products were misbranded by respondents in that they were not stamped, tagged, labeled or otherwise identified as required under the provisions of Section 4(b) of the Textile Fiber Products Identification Act, and in the manner and form as prescribed by the rules and regulations promulgated under said Act.

Among such misbranded textile fiber products, but not limited thereto, were textile fiber products with labels which failed:

(1) To disclose the true generic names of fibers present; and

(2) To disclose the true percentages of such fibers.

PAR. 5. Respondents' textile fiber products described in Paragraph Four above were imported by the respondents into the United States and, as particularized in said paragraph, were not stamped, tagged, labeled, or otherwise identified in accordance with the provisions of the Textile Fiber Products Identification Act. The invoices of said imported textile fiber products required by the Tariff Act of 1930 failed to set forth the information with respect to said textile fiber products required under Section 4(b) of the Textile Fiber Products Identification Act. The respondents did falsify the consignee's declaration provided for in said Tariff Act of 1930 insofar as it related to said information, in violation of Section 9 of the Textile Fiber Products Identification Act and Section 5 of the Federal Trade Commission Act.

PAR. 6. The acts and practices of respondents as set forth in Paragraphs Three, Four and Five above were, and are, in violation of the Textile Fiber Products Identification Act and the rules and regulations promulgated thereunder, and constituted, and now constitute, unfair methods of competition [5] and unfair and deceptive acts and practices, in commerce, under the Federal Trade Commission Act.

PAR. 7. Respondents now and for some time past have imported for introduction into commerce, introduced into commerce, sold, transported, distributed, delivered for shipment, shipped and offered for sale, in commerce, as "commerce" is defined in the Wool Products Labeling Act of 1939, wool products, as "wool product" is defined therein.

PAR. 8. Certain of said wool products were misbranded by respondents within the intent and meaning of Section 4(a)(1) of the

Wool Products Labeling Act of 1939 and the rules and regulations promulgated thereunder, in that they were falsely and deceptively stamped, tagged, labeled, or otherwise identified with respect to the character and amount of the constituent fibers contained therein.

Among such misbranded wool products, but not limited thereto, were certain wool fabrics stamped, tagged, labeled, or otherwise identified by respondents as "45% acrylic, 30% wool, 25% cotton" whereas, in truth and in fact, said products contained substantially different fibers and amounts of fibers than represented.

PAR. 9. Certain of said wool products were further misbranded by respondents in that they were not stamped, tagged, labeled, or otherwise identified as required under the provisions of Section 4(a)(2) of the Wool Products Labeling Act of 1939 and in the manner and form as prescribed by the rules and regulations promulgated under said Act.

Among such misbranded wool products, but not limited thereto, were wool products, namely wool fabrics, with labels on or affixed thereto, which failed to disclose the percentage of the total fiber weight of the said wool products, exclusive of ornamentation [6] not exceeding 5 per centum of said total fiber weight, of (1) wool, (2) reprocessed wool, (3) reused wool, (4) each fiber other than wool, when said percentage by weight of such fiber was 5 per centum or more, and (5) the aggregate of all other fibers.

PAR. 10. Respondents' wool products described in Paragraph Nine above were imported by the respondents into the United States and, as particularized in said paragraph, were not stamped, tagged, labeled, or otherwise identified in accordance with the provisions of the Wool Products Labeling Act of 1939. The respondents in their invoices of said imported wool products required by the Tariff Act of 1930 failed to set forth the information with respect to said wool products required under the provisions of the Wool Products Labeling Act of 1939, to wit, the percentage of the total fiber weight of the said wool products, exclusive of ornamentation not exceeding 5 per centum of said total fiber weight, of (1) wool, (2) reprocessed wool, (3) reused wool, (4) each fiber other than wool, when said percentage by weight of such fiber was 5 per centum or more, and (5) the aggregate of all other fibers. The respondents did falsify the consignee's declaration provided for in said Tariff Act of 1930 insofar as it related to the above items of information enumerated in this paragraph, in violation of Section 8 of the Wool Products Labeling Act of 1939 and Section 5 of the Federal Trade Commission Act.

PAR. 11. The acts and practices of the respondents as herein alleged in Paragraphs Eight, Nine and Ten were, and are, in violation of the Wool Products Labeling Act of 1939 and the rules and regulations promulgated thereunder, and constituted, and now constitute, unfair methods of competition and unfair and deceptive acts and practices, in commerce, within the meaning of the Federal Trade Commission Act. [7]

PAR. 12. Respondents, now and for some time past, have been engaged in the importation, offering for sale, sale, and distribution of certain products, namely fabrics. In the course and conduct of their business as aforesaid, respondents now cause and for some time past have caused their said products, when sold, to be shipped from the State of New York to purchasers located in various other States of the United States, and maintain and at all times mentioned herein have maintained, a substantial course of trade in said products in commerce, as "commerce" is defined in the Federal Trade Commission Act.

PAR. 13. In the course and conduct of their business, respondents have misrepresented to their customers the character and amount of the constituent fibers contained in their products through falsely and deceptively stamping, tagging, labeling and otherwise identifying said products.

Among such products, but not limited thereto, were fabrics labeled as "65% acrylic, 25% cotton, 10% nylon" whereas, in truth and in fact, such products contained substantially different fibers and amounts of fibers than represented including wool.

PAR. 14. In the course and conduct of their business, respondents have misrepresented to their customers the shrinkage factor of their textile products through falsely and deceptively invoicing said products.

Among such products, but not limited thereto were fabrics represented as having 1-1 1/2% residual shrinkage whereas, in truth and in fact, such products shrink substantially more than represented.

PAR. 15. Respondents in the course and conduct of their business have made statements on [8] invoices to their customers, misrepresenting the fiber content of certain of their products.

Among such misrepresentations, but not limited thereto, were statements setting forth the fiber content thereof as "55% acrylic, 20% wool, 20% cotton, 5% other fibers" whereas, in truth and in fact, said products contained substantially different fibers and amounts of fibers than represented.

PAR. 16. The aforesaid acts and practices of respondents as herein alleged in Paragraphs Thirteen, Fourteen and Fifteen were and are, all to the prejudice and injury of the public and constituted, and now constitute, unfair methods of competition and unfair and deceptive acts and practices, in commerce, within the intent and meaning of the Federal Trade Commission Act.

INITIAL DECISION BY PAUL R. TEETOR, ADMINISTRATIVE LAW JUDGE

NOVEMBER 25, 1977

I

SUMMARY OF COMPLAINT

Identification of Respondents

Alleging violations of the Wool Products Labeling Act of 1939 (hereafter "the Wool Act"), the Textile Fiber Products Identification Act (hereafter "the Textile Act") and Section 5 of the Federal Trade Commission Act (hereafter "the FTC Act") and the rules and regulations promulgated thereunder, on 6/24/75 this Commission issued its complaint against what *Paragraph 1* thereof alleges to be "a unified family business operation." It is said to be made up of Verrazzano Trading Corporation, Francesco Datini Inc., Lanificio Tuscania Inc., Lima Textiles Inc. (all New York corporations with an office in New York City) and one Walter Banci, personally, as an officer and agent for said corporations and as a partner in an Italian company, Lanificio Walter Banci s.a.s. His wife, Lola Conti Banci, is alleged to be an inactive partner. [An amendment to the complaint allowed by the administrative law judge without objection on 2/10/76 added Hudson Textile, Inc. (also a New York corporation) as an additional respondent and alleged participant in the same enterprise.] This "unified family business" is alleged in Paragraph 1 to be designed to import and sell in the United States and distribute in "commerce" their fabrics produced and exported from Italy by Lanificio Walter Banci s.a.s.

"Commerce" Allegations

Complaint Paragraph 2 alleges that respondents engage in importing, transporting, advertising, offering and selling *textile fiber products* and introducing them in "commerce," both phrases being defined as in the Textile Fiber Products Identification Act (hereafter the "Textile Act"). [2]

Paragraph 7 alleges that respondents engage in importing, transporting, distributing, offering, selling, shipping and delivering *wool products* and introducing them in "commerce" (both phrases being defined as in the Wool Products Labeling Act (hereafter the "Wool Act").

Paragraph 12 alleges that respondent engage in importing, distributing, offering and selling *fabrics generally,* shipping such fabrics, when sold, from the State of New York to purchasers located in various states, the same amounting to a "substantial course of trade" in "commerce," as defined in the Federal Trade Commission Act (hereafter the "FTC Act").

Alleged Violations of the Textile Act

Complaint Paragraph 3 pleads a violation of Section 4(a) of the Textile Act, which prohibits "misbranding," *i.e., false and deceptive identification of the name or amount of constituents in textile fabrics.* An example of such misbranding is said to be the identification of a textile fabric as "50% cotton, 35% polyester, 15% nylon" when the constituent fibers and amounts thereof are, in fact, "substantially different."

Complaint Paragraph 6 adds that such violation of Section 4(a) of the Textile Act, by virtue of Section 7 thereof, automatically constitutes, in addition, an unfair practice under the FTC Act.

Complaint Paragraph 4 pleads a violation of Section 4(b) of the Textile Act, which prohibits "misbranding" *i.e., non-attachment or non-affixation of specified identifying data of textile fiber products.* An example of such misbranding is said to be the non-disclosure on textile fiber product labels of the true generic names of fibers present or the true percentages of such fibers therein contained.

Complaint Paragraph 6 adds that such violation of the Textile Act, by virtue of Section 7 thereof, automatically constitutes, in addition, an unfair practice under the FTC Act. [3]

Complaint Paragraph 5 pleads a violation of Section 9 of the Textile Act, which prohibits *importation into the United States of textile fiber products "misbranded" under Section 4 of the act* (above). In elaboration, Paragraph 5 explains that the required identifying information was omitted from so-called *Tariff Act invoices* and falsified on so-called *Tariff Act consignee-declarations.*

Complaint Paragraph 6 adds that such violation of Section 9 of the Textile Act, by virtue of Section 7 thereof, automatically constitutes, in addition, an unfair practice under the FTC Act.

Alleged Violations of the Wool Act

Complaint Paragraph 8 pleads a violation of Section 4(a)(1) of the Wool Act, which prohibits *false and deceptive identification ("misb-*

randing") of wool products. An example of such misbranding is said to be the identification of certain wool fabrics as "45% acrylic, 30% wool, 25% cotton," whereas said fabrics in fact contained "substantially different" fibers or amounts of fibers. *Complaint Paragraph 11* adds that such violation of the Wool Act, by virtue of Section 6 thereof, automatically constitutes, in addition, an unfair practice under the FTC Act.

Complaint Paragraph 9 pleads a violation of Section 4(a)(2) of the Wool Act, which prohibits *non-attachment or non-affixation of specified identifying data ("misbranding") of wool products.* An example of such misbranding is said to be failure to disclose by a label on or affixed to a wool product the percentage of total fiber weight[1] which is: [4]

(1) wool
(2) reprocessed wool
(3) re-used wool
(4) each non-wool fiber representing 5% or more of total weight
(5) the aggregate of all other fibers.

Complaint Paragraph 11 adds that such violation of the Wool Act, by virtue of Section 6 thereof, automatically constitutes, in addition, an unfair practice under the FTC Act.

Complaint Paragraph 10 pleads a violation of Section 8 of the Wool Act, which prohibits *importation into the United States of wool products "misbranded" under Section 4 of the act* (above). In elaboration, Paragraph 10 explains that required identifying information was omitted from so-called *Tariff Act invoices* and falsified on so-called *Tariff Act consignee-declarations. Complaint Paragraph 11* adds that such violation of the Wool Act, by virtue of Section 6 thereof, automatically constitutes, in addition, an unfair practice under the FTC Act.

Alleged Violations of Federal Trade Commission Act[2]

Complaint Paragraph 13 pleads a violation of Section 5 of the FTC Act, which prohibits unfair and deceptive trade practices, alleging *misrepresentation of the character and amount of constituent fibers in respondents' fabrics.* An example pleaded is the [5] labeling of fabrics "65% acrylic, 75% cotton, 10% nylon," whereas, in fact, such fabrics contained "substantially different" kinds and amounts of fibers, including wool.[3]

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[1] Exclusive of ornamentation not exceeding 5% of total fiber weight.

[2] *Complaint Paragraphs 13, 14 and 15* plead unfair trade practices under Section 5 of the FTC Act which do *not* (unlike earlier allegations of unfair practices) derive automatically from a Textile Act or Wool Act violation and which, in fact, for one reason or another, could not have been made the basis for a Textile Act or Wool Act charge. The "public interest" finding requisite to all three FTC Act charges is pleaded in *complaint Paragraph 16.*

Complaint Paragraph 14 pleads a violation of Section 5 of the FTC Act, which prohibits unfair and deceptive trade practices, alleging *misrepresentation of the shrinkage factor*[4] *in respondents' textile products.* An example pleaded is a representation that fabrics have 1-1 1/2% residual shrinkage whereas, in truth, such fabrics shrink "substantially more" than represented.

Complaint Paragraph 15 pleads a violation of Section 5 of the FTC Act, which prohibits unfair and deceptive trade practices, alleging *misrepresentation by means of commercial (i.e., non-Tariff Act) invoices*[5] concerning certain products' fiber content. An example pleaded is a representation that fiber content is [6] "55% acrylic, 20% wool, 20% cotton, 5% other fibers," whereas, in fact, such products contain "substantially different" kinds and amounts of fibers than represented.

Complaint Paragraph 16 pleads the public interest in prosecution which must exist to justify bringing charges (as in Paragraphs 13, 14 and 15) under Section 5 of the FTC Act (as distinguished from either the Wool Act or Textile Act).

Proposed Order

A proposed order, served with the complaint, contemplates cease and desist orders against all respondents, which orders would prohibit: (1) misbranding textile fiber products by false or deceptive identification of the name or amount of constituent fibers or by failing to affix each element of information required by Section 4(b) of the Textile Fiber Products Identification Act; (2) importing textile fiber products into the United States except upon filing a bond in double import value to comply with the Textile Fiber Products Identification Act; (3) misbranding wool products by false or deceptive identification of the character or amount of constituent fibers or by failing to affix each element of information required by Section 4(a)(2) of the Wool Products Labeling Act; (4) importing wool products into the United States except upon filing a bond in double import value to comply with the Wool Products Labeling Act; (5) misrepresenting the character or amount of constituent fibers or the shrinkage factor of wool and/or textile products in any manner, including identification in invoices.

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[3] The significance of wool traces lies in making such a fabric a "wool product" and thus exempt from application of the Textile Act, at least according to complaint counsel's reasoning, as will be discussed at page 32 below.

[4] A misrepresentation concerning a fabric's shrinkage potential must be pleaded under the FTC Act because both the Textile Act and the Wool Act are concerned only with the kinds and quantities of fibers contained in a fabric.

[5] Misrepresentation of the fiber content of a wool product must be charged under the FTC Act if the instrumentality of the misrepresentation is an ordinary commercial invoice (as distinguished from a so-called Tariff Act invoice) because the Wool Act (as distinguished from the Textile Act) does not reach misrepresentation by means of a commercial invoice.

Respondents would also be required to give notice of misbranding to those customers who have bought misbranded products; to notify this Commission of changes in business affiliation or employment; to give notice to the Commission 30 days before making any structural change in their business which might affect compliance with this order; and to distribute copies of this order throughout their organization. [7]

II

PROCEDURAL HISTORY

From the issuance of the Commission's complaint on 6/24/75 to the filing of this initial decision on 11/25/77, a period of nearly two and a half years has elapsed. To one uninitiated in the lengthy discovery procedures and complex motion practice that have come to characterize Commission proceedings for the purpose of satisfying the requirements of due process of law for businessmen, it might appear that the administrative law judge and the parties put this relatively small and largely indefensible[6] case on the back burner for many months at a time.

On the contrary, the two and a half years were crowded with constant motions and discovery procedures. Aside from an inexplicable delay by the contract reporter of more than three months in correcting the pagination and other clerical errors of this relatively small trial transcript, there was almost never a period of time when some pre-trial, trial or post-trial procedure was not in the offing.

Lest there be any question on this score, we have compiled a detailed procedural history of this matter which is attached hereto as Appendix I, to which any reader interested in the facts of this case or any student interested in its implications for the future of administrative jurisprudence is hereby referred. We now turn directly to our findings of fact, which are notably briefer than the procedural history of their evocation. [8]

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[6] On 11/16/76, respondents' counsel stated frankly in open court: "Now my fight will have to be a weak one since I have nothing to show on Banci's side but I still have the right to put the Commission to its proof." (Tr. 76.)

III

FINDINGS OF FACT

Parties

1. The sole individual respondent and principal figure in this matter is Walter Banci, partner with his wife, Lola Conti Banci, in a business known as Lanificio Walter Banci s.a.s. (Original Complaint; Ans. I, § 1; Ans. II, § 1; Ans. III, § 1), a firm which operates two textile mills near Prato, Italy (Tr. 78).

2. For some years Banci has sold his textiles in the United States through several corporations, all organized and existing under the laws of New York. (Original Complaint; Ans. I, § 1; Ans. II, § 1; Ans. III, § 1).

3. Four of these New York corporations were named as respondents in the original complaint here:

Verrazzano Trading Corp. (hereafter "Verrazzano")
Francesco Datini Inc. (hereafter "Datini")
Lanificio Tuscania Inc. (hereafter "Tuscania")
Lima Textiles Inc. (hereafter "Lima")
(Original Complaint; Ans. I, § 1; Ans. II, § 1; Ans. III, § 1)

4. A fifth corporation, named Hudson Textile Corporation (hereafter "Hudson"), also organized and existing under the laws of New York, was subsequently joined as a respondent without objection (Amended Complaint; Ans. III, § 1; failure of original respondents to deny amended complaint). [9]

5. All respondents together have constituted a unified family business operation designed to import and sell in the United States wool and textile products manufactured by Lanificio Walter Banci s.a.s. (RA I, ¶ 642; Amended Complaint and Ans. III, § 1; see also an earlier *Verrazzano* case, reported in 1971 in 78 F.T.C. 637, at 668.

6. Respondent Banci has formulated, directed and controlled the acts and practices of this unified family business operation, both the Italian family partnership (Lanificio Walter Banci s.a.s.) and the American corporate respondents, including the acts and practices challenged in the complaint here. (RA I, ¶ 641; Complaint § 1; Ans. I, § 1; Ans. II, § 1; Amended Complaint § 1; Ans. III, § 1). As his counsel put it: ". . . Mr. Banci's operation is such that he really is the man who does everything. . ." (Tr. 77).

7. All respondents were actively doing business from an office at 2 Penn Plaza in New York City (their only office in the United States, on this record) at least from 1/1/69 through 9/1/75 (ALJ's "Application Of Sanctions Under Rule § 3.38 For Failure Of

Respondents To Make Discovery As Ordered," dated 4/16/76, at pp. 6-7.)

8. During the years in question here, respondents admit, fabric manufactured by Lanificio Walter Banci s.a.s. was shipped to the United States in substantial quantities (Tr. 58). Moreover, we have earlier found that since January 1972 and for the time period covered by the complaint respondents have maintained a substantial course of trade in wool and textile products in the United States. ("ALJ's Application Of Sanctions Under Rule § 3.38 For Failure Of Respondents To Make Discovery As Ordered," dated 4/16/76, at pp. 4-6.) We have further found that since January 1972 respondents have sold to United States customers substantial quantities of each of many specific textile products (including qualities Sioux, Manito, Totem, Veruska, Navajo, Ingrid and Myla) and wool products (including qualities Marnie, Gretel, Isabel, Spluga, Eva, and Ellen). [10] (ALJ's "Application Of Sanctions Under Rule § 3.38 For Failure Of Respondents To Make Discovery As Ordered," dated 4/16/76, at pp. 4-6.)

9. It is conceded by complaint counsel that after issuance of this complaint and at least by November 1976, respondents were no longer doing business in the United States and that their New York City office was closed by then. (Tr. 78.)

10. This record is barren of evidence, however, as to whether Banci may or may not resume his American sales, either through the present corporate respondents or through other vehicles.[7]

Importation and Sale in Commerce

11. All the original respondents, including Walter Banci, in their Answers admitted the allegations of complaint Paragraphs 2, 7 and 12,[8] [11] concerning respondent's engagement in the importation of

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[7] Subsequent to the closing of the record here both sides made claims on this subject but neither moved to reopen the record to take further evidence. When submitting his proposed findings, counsel for respondents reported (but without benefit of affidavit) that Lanificio Walter Banci s.a.s. was adjudicated bankrupt in Prato, Italy on 9/2/77. Complaint counsel countered by attaching to their reply brief unverified copies of Customs records of a Banci sale to a New York customer as late as 9/29/77. We view both submissions as improper and we shall attach no weight to either.

[8] The complaint allegations thus admitted are as follows:

"Paragraph Two: Respondents are now and for some time past have been engaged in the introduction, sale, advertising, and offering for sale, in commerce, and in the transportation or causing to be transported in commerce, and in the importation into the United States, of textile fiber products; and have sold, offered for sale, advertised, delivered, transported and caused to be transported, textile fiber products which have been advertised or offered for sale in commerce, and have sold, offered for sale, advertised, delivered, transported, and caused to be transported after shipment in commerce, textile fiber products as the terms "commerce" and "textile fiber product" are defined in the Textile Fiber Products Identification Act."

"Paragraph Seven: Respondents now and for some time past have imported for introduction into commerce, introduced into commerce, sold, transported, distributed, delivered for shipment, shipped and offered for sale, in commerce, as "commerce" is defined in the Wool Products Labeling Act of 1939, wool products, as "wool product" is defined therein."

(Continued)

textile fiber and wool products into the United States and their sale and shipment, etc. thereof from New York to other states, in [12] commerce, as "commerce" is defined in the Wool, Textile and FTC Acts. (Original Complaint; Ans. I, § 2; Ans. II, § 2).

12. When Hudson Textile Corporation was subsequently joined as a respondent, its Answer to the amended complaint, for no reason that has yet become apparent, denied the commerce allegations found in complaint Paragraphs 2, 7 and 12.[9] However, respondent Hudson's Answer to the amended complaint admitted most of the allegations of complaint Paragraph 1, including an allegation that "the corporate respondents" — which by then included Hudson — together with respondent Banci, constituted "a unified family business operation designed to import and sell in the United States fabrics produced and exported from Italy by Lanificio Walter Banci s.a.s. and distribute such fabrics in commerce." (Complaint, § 1; "Order Granting Amendment Of The Complaint," dated 2/9/76; Ans. III, § 1). As a part of this "unified family business operation," respondent Hudson, was necessarily engaged in the business' importation of wool and textile products from Italy into the United States and the sale, shipment, etc. of such products "in commerce" from New York to other states and we now so find.

Investigation of Possible Misbranding

13. In 1971 this Commission agreed to dismiss misbranding charges against most of the same respondents on condition that they would voluntarily comply with the misbranding laws. See *Verrazzano Trading Corporation t/a Lan Etruria, et al.*, 78 F.T.C. 637, 675 (1971).

14. Between 1973 and 1975 the Commission conducted a new investigation into possible misbranding by respondents of woolen and other textiles imported from Italy into the United States and thereafter distributed in interstate commerce. [13]

Sample Sources

15. Many samples of respondents' imported fabrics were obtained from the United States Customs Service in New York City and many

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"Paragraph Twelve: Respondents, now and for some time past, have been engaged in the importation, offering for sale, sale, and distribution of certain products, namely fabrics. In the course and conduct of their business as aforesaid, respondents now cause and for some time past have caused their said products, when sold, to be shipped from the State of New York to purchasers located in various other States of the United States, and maintain and at all times mentioned herein have maintained, a substantial course of trade in said products in commerce, as "commerce" is defined in the Federal Trade Commission Act."

[9] See preceding footnote.

others were obtained from United States customers of respondents, including the following:

Bobbie Brooks, Inc., 3830 Kelley Ave., Cleveland, Ohio (Tr. 374–75)

Ivy International, Ltd., 119 W. 40th St., New York, N.Y. (RA II, ¶ 45, ¶ 150, ¶ 170; RA III, ¶ 28)

MelRose Mfg. Co., 712 Commerce St., Dallas, Texas (RA II, ¶ 1, ¶ 2; RA III, ¶ 17, ¶ 18)

Jones of Dallas Mfg., Inc., 2316 N. Griffin St., Dallas, Texas (RA II, ¶ 15, ¶ 16; RA III, ¶ 19, ¶ 20)

Abbott Fabrics, Inc., 1412 Broadway, New York, N.Y. (RA II, ¶ 47, ¶ 48, ¶ 49; RA III, ¶ 21, ¶ 22, ¶ 23)

Artbro Sportswear, Inc., 1407 Broadway, New York, N.Y. (RA II, ¶ 88; RA III, ¶ 25)

F. Resnick, Inc., 242 W. 39th St., New York, N.Y. (RA II, ¶ 107; RA III, ¶ 26)

Fabri-Centers of America, Inc., 23550 Commerce Park, Beachwood, Ohio (RA I, ¶ 19; RA III, ¶ 2)

Sample Quantity

16. Although respondents concede that their total imports of wool and other textile products into the United States during the period in question were "substantial" (Tr. 58), they have declined to [14] provide data on the total quantities[10] imported. It is therefore impossible, because of respondents' contumacy, to determine with any precision what percentage of their total imports during that period have been sampled.

17. However, the record shows that 58 undisputed samples were taken (RA I, ¶ 19, ¶ 38, ¶ 55; RA II, ¶ 1, 2, 15–18, 47–49, 87–88, 107–8, 145; RA III, ¶ 1–30; RA V, ¶ 1–40) and that the shipments from which they were taken totaled over 1,185,000 yards of woolen and other textile products. [Of this total, customs samples account for about 550,000 yards (see App. II. Col.) and one customer (Bobbie Brooks, Inc.) for 635,000 yards. (Tr. 374–375).]

18. We find that the woolen and other textile products from which the above samples were taken represent a very substantial

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[10] Respondents did reveal that the *value* of their imports to the United States was 1.424 billion lire in 1974 and .271 billion lire in 1975. At the exchange rate as published (.001543) in the "Bank & Quotation Record Magazine," of January 1975, these figures would convert to 2.2 million dollars and .4 million dollars, respectively.

amount of trade in and of themselves and, drawing an inference permissible under Rule 3.38[11] that withheld evidence would have been unfavorable, we find further that the goods sampled were quite probably a substantial portion of respondents' total imports during the period in question.

Testing Process

19. The 58 samples listed in Appendix II were each subjected to testing for actual fiber content, in some cases by the U.S. Customs laboratory technicians and in others by independent experts employed for that purpose by this Commission. The tests employed and their validity were the subject of testimony by three expert witnesses: [15]

20. *Dr. Samuel Golub,* a 20-year veteran of textile research, currently in charge of fabric analysis for Fabric Research Laboratories, Dedham, Mass. (Tr. 105–06); *Ms. Amelia Eaton,* holder of a degree in textile chemistry, veteran of fabric analysis, and currently laboratory director for the U.S. Customs Service (Tr. 205–06). Both she and Dr. Golub have been active in the American Society of Testing Materials (hereafter "ASTM") and the American Society of Textile Chemists and Colorists (hereafter "AATCC"), associations that have developed standard methods for qualitative and quantitative textile fiber analysis (Tr. 106–7, 118, 208); *Mr. Martin Youngberg,* holder of a degree in textile technology, has for eight years been a chemist in the fiber branch of the U.S. Customs Service laboratory, performing fiber content analyses throughout that time. (Tr. 330.)

21. All three witnesses described very similar procedures for analysis of fabric samples. Dr. Golub tested CX 5, 9 through 13, 19 through 28, and CX 30. He testified that in his opinion CX 112 a–f accurately represents the results of his testing. (Tr. 107–09.) He explained a typical multi-fiber analysis at the hearing. [The exact process for each test, he noted, may be different because of different fibers present in the sample. (Tr. 150.)]. He began by preparing two specimens so that he could run two separate tests on each sample. (Tr. 130.) He examined microscopic slides of the sample to identify the fibers present and thus determine the particular chemical sequence to be used to decipher the percentage weight of each fiber. (Tr. 136.)

22. Thereafter, Dr. Golub explained, the procedure is to extract the spinning oils from the fabric; dry and weigh the fabric; apply a reagent grade chemical which will dissolve one of the fibers; and

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[11] The drawing of such an inference was expressly left open in the ALJ's order of 4/19/76, page 7.

repeat the process until all fibers have been dissolved except one. (Tr. 136–142.) More specifically, Dr. Golub testified that if he identified fibers of acrylic, nylon, wool, cotton, rayon, and polyester, he would use cold dimethyl [16] formamide to remove acrylics, formic acid to remove the nylon, 5% sodium hydroxide to remove wool, 70% sulphuric acid to remove the cotton and rayon, with the remainder being polyester. The sample would be rinsed, dried and weighed between each application of a reagent. (Tr. 139–142.)

23. Ms. Eaton described similar procedures used at the U.S. Customs Laboratory where, just as with Dr. Golub's work, all tests are done in duplicate. (Tr. 210.) She explained that the chemists, who all work under her general supervision, use microscopic analysis to determine what fibers are present in the fabric and to devise an appropriate chemical sequence. (Tr. 212.) They then extract spinning oils and other non-fibrous material from the sample. (Tr. 213.) After the initial weighing under controlled temperature conditions, reagents are applied to the sample to remove a fiber. Then the sample is again rinsed, dried and weighed under constant conditions. (Tr. 243–44.) Specifically, Ms. Eaton suggested using sodium hypochlorite to dissolve wool (Tr. 250–51); dimethyl formamide to remove acrylics and acetate (Tr. 256); formic acid to remove nylon (Tr. 257); and 59.5% sulphuric acid to remove rayon (Tr. 257). Samples tested under the supervision of Ms. Eaton are CX 4, 31–33, and 35–71. The corresponding test reports are CX 154, 113, 114, 115, and 117–153. Respondents' counsel agreed that the above-listed exhibits are genuine U.S. Customs' laboratory reports of analyses done on the samples. (Tr. 215–16.)

24. Mr. Youngberg was the chemist who personally performed many of the tests cited above. (Tr. 330; CX 123, 129, 130, 135, 136, 140, 141, 142, 151, 152, 154.) The reports accurately represented his findings of his analyses according to Customs procedures. (Tr. 331.) He described the procedures he followed. He removed two specimens from each sample to run duplicate tests. He then began by removing non-fibrous material, then dried the sample, ground it up, mixed it and conditioned it. [17] He microscopically examined the sample to identify the fibers present and determined the "scheme of attack." (Tr. 335.) He would use either AATCC or established Customs methods (Tr. 335–37), that is, sodium hypochlorite for removing wool (Tr. 341); dimethyl formamide for dissolving acrylic and acetate (Tr. 324); formic acid to remove nylon (Tr. 341); 59.5% sulphuric acid for rayon (Tr. 342); 70% sulphuric acid for cotton. This procedure would leave a residue of polyester. (Tr. 324.)

24.1. There is no single standard chemical sequence to follow for multifiber analysis. Dr. Golub testified that correct results can be obtained from several different methods, explaining that "[t]he only requirement is that the operator should know that and assure himself that his is not losing weight from one of the subsequent fibers which has not yet been dissolved by any particular step of the process." (Tr. 159.) Both Dr. Golub and Ms. Eaton have checked their fiber analysis methods for accuracy. (Tr. 150–51, 214.) Dr. Golub used acceptable methods for testing the samples given him by complaint counsel. (Tr. 158.) Mr. Youngberg followed regular Customs procedures, developed by Ms. Eaton, in testing the samples assigned to him. (Tr. 214, 331.) A stipulation was agreed to by the parties that, as to the remaining samples, the chemists performing the analyses would testify that they, too, followed regular Customs procedures. (Tr. 361.) Accordingly, we find that the samples reported in Appendix II were all tested in accordance with reasonable and scientifically acceptable chemical procedures and that the results of the tests are satisfactory evidence of the true fiber content of the samples. [17.1]

24.2. From time to time, respondents' counsel has alluded to the possibility that fabrics manufactured in Italy were made from used fibers and that this would affect test results. Beyond respondents' counsels' innuendo there is no evidence that used fibers were actually used in respondent Banci's mills, let alone in the particular runs involved here. In any event both experts Golub and Eaton testified that the presence of used fibers in the samples would not materially affect the fiber analysis. Even assuming that such a possibility existed, the testing chemist would recognize it and make corrections in the test accordingly. (Tr. 128, 286, 287.) We find that the speculative suggestions of respondents' counsel in this regard are without substance, at least as far as this record is concerned.

25. In assessing the deviations from respondents' representations concerning fiber content summarized in Appendix II, it should be borne in mind that this Commission, by regulation, will not deem such deviation "misbranding" if it does not exceed 3% (by weight) of a textile product's total fiber content. 16 C.F.R. 303.43(a).

Test Results

26. The results of the fiber content tests of these 58 fabric samples are embodied in Appendix II. Each sample is there denoted by its exhibit number, manufacturer's "quality", quantity of the source fabric, source of data (Customs or customer), year of shipment, represented fiber content, tested fiber content and deviation of actual fiber content from [18] that represented

(expressed in percentage points above or below the representation). We find Appendix II to be an accurate statement of the facts it purports to show.

27. For purposes of analysis the 58 fabric samples whose characteristics are summarized in Appendix II are broken down into three groups. *Group I* includes 24 fabric samples which were represented by respondents to contain certain percentages of various textile fibers, but none of which samples were claimed to include or in fact turned out to include any wool. *Group II* includes 25 fabric samples which were represented by respondents to contain certain percentages of textile fibers, all of which samples were claimed to include and, in fact, turned out to include certain percentages of wool. *Group III* includes 9 fabric samples which were represented by respondents to contain certain percentages of various textile fibers, none of which samples, however, were claimed to include any wool but all of which, in fact, turned out to include at least traces of wool.

28. *Group I.* This group of 24 textile samples, as to which no wool content was either claimed or found by testing, reveals serious and pervasive misbranding. Of primary interest is misbranding which *overstates* fiber content. Disregarding 8 fiber overstatements of 3% or less as being within the tolerance of 16 C.F.R. 303.43(a), we find 29 other fiber overstatements, each in excess of 3% of total fiber weight. The number and magnitude of these overstatements was as follows:

Group I

Non-Wool Textiles

Magnitude of overstatements	*Number of overstatements*
3 to 10 percentage points	9
10 to 20 percentage points	12
over 20 percentage points	8
Total overstatements (over 3%)	29

[19] 29. As discussed later (p. 31 below), there is a question whether misbranding which merely *understates* fiber content violates the Textile or Wool Acts. The facts here reveal a considerable number of such understatements. Disregarding 1 understatement of less than 3%, we find 38 other fiber understatements, each in excess of 3% of total fiber weight. The number and magnitude of these understatements were as follows:

Group I

Non-Wool Textiles

Magnitude of understatements	*Number of understatements*
3 to 10 percentage points	16
10 to 20 percentage points	19
over 20 percentage points	3
Total understatements (over 3%)	38

29.1. We also find that in Group I, there were three instances (CX 61, 62, 63) where testing revealed the presence of acrylic in amounts over 5% of the total fiber weight of the sample and yet acrylic was not revealed by respondents to be a constituent fiber.

30. *Group II.* This group of 25 fabric samples, each of which was represented to include and did include some wool, also reveals serious and pervasive misbranding. It is desirable to analyze the extent of deviation from represented fiber content in this group of textile samples not only in terms of overstatements vs. understatements (as in Group I) but also in terms of wool fiber vs. all other fibers, for the legal consequences vary, depending on these factors.

31. *Wool fiber content.* There were no *understatements* of wool fiber content in any of the 25 samples in Group II but all 25 samples revealed *overstatements* of wool content, in almost all instances (23) by over 10 percentage points. The number and magnitude of wool fiber overstatements were as follows:

Group II

Wool Fiber

Magnitude of overstatements	*Number of overstatements*
3 to 10 percentage points	2
10 to 20 percentage points	23
over 20 percentage points	0
Total overstatements (over 3%)	25

[20] 32. *Other (non-wool) fibers.* The 25 textile samples in Group II reveal a substantial number of deviations from represented content, both overstatements and understatements, of fiber constituents other than wool. Disregarding 2 overstatements of less than 3%, the

number and magnitude of all other non-wool fiber *overstatements* were as follows:

Group II

Non-Wool Fibers

Magnitude of overstatements	***Number of overstatements***
3 to 10 percentage points	**13**
10 to 20 percentage points	**6**
over 20 percentage points	**10**
Total overstatements (over 3%)	**29**

33. There were also a number of *understatements* of the content of the non-wool textile fibers of Group II. Disregarding 7 understatements of less than 3%, their number and magnitude were as follows:

Group II

Non-Wool Fibers

Magnitude of understatements	***Number of understatements***
3 to 10 percentage points	**8**
10 to 20 percentage points	**4**
over 20 percentage points	**0**
Total understatements (over 3%)	**12**

33.1. We also find in Group II fibers were included in the wool products which were not revealed on respondents' fiber content tags. CX 19, 20, 21, 23, 24, 25, 26, 27, 28, 31, 32, 35, 36, 39, 41 and 42 all contained nylon and polyester, each in amounts of over 5% of the total fiber weight of the product but were claimed by respondents to contain only wool, cotton and acrylic. CX 22, 37, 38, 40 and 4 contained nylon in amounts over 5% of the total fiber weight.

34. *Group III.* This relatively small group of 9 textile samples is significant largely because it poses the unusual situation of textiles not *claimed* to contain any wool but *found* on testing to contain at least traces of wool (and, for that reason, pleaded here as [21] direct[12] violations of the FTC Act rather than as derived from either the

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[12] The Group I and Group II situation, too, are alleged to constitute violations of the FTC Act but only a *derivative* theory. If a Textile Act and/or Wool Act charge fails in those situations, the *derivative* FTC Act charge would presumably fail automatically. Contra as to Group III situations.

Wool Act or the Textile Act.) The wool traces, found in *each* Group III textile sample, range from 1.1% to 9.6%, averaging 3.5%.

35. Disregarding 2 overstatements of less than 3%, Group III contains a number of substantial *overstatements* of non-wool fiber content as follows:

Group III

Textiles Containing Unclaimed Wool

Magnitude of overstatements	*Number of overstatements*
3 to 10 percentage points	5
10 to 20 percentage points	6
over 20 percentage points	5
Total overstatements (over 3%)	16

In addition to one understatement of less than 3%, Group III also contains a number of *understatements* of non-wool fiber content as follows:

Group III

Textiles Containing Unclaimed Wool

Magnitude of understatements	*Number of understatements*
3 to 10 percentage points	2
10 to 20 percentage points	1
over 20 percentage points	5
Total understatements (over 3%)	8

[22] 36. *Residual Shrinkage.* In 1973 and 1974 respondents sold approximately 790,000 yards of fabric (qualities Sioux, Totem and Manito) to Bobbie Brooks, Inc. Bobbie Brooks actually received 635,000 yards which were used in the manufacture of 25,000 dozen garments. (Tr. 374–75.) Respondents' sales invoices for qualities Sioux and Totem represented that the fabric had a residual shrinkage of from one to one and a half percent. (RA I, ¶ 43.) Several samples of this fabric (CX 15, 16, 17, 18) were tested by Dr. Golub for residual shrinkage. (Tr. 109.) Respondents admitted that the samples tested were samples of fabrics manufactured, sold and shipped by them. (RA I, ¶ 38; RA III, ¶ 13, 14, 15, 16.) Dr. Golub's tests indicated and we now find that the actual residual shrinkage of the samples

was approximately 5-6%, substantially more than respondents' claim of 1 to 1 1/2% (CX 112d; Tr. 110) and also substantially more than the maximum of 3 1/2% permitted for such fabrics by the American National Standards Institute (Tr. 111).

37. Dr. Golub testified that washing has little effect on clothing manufactured from fabrics having a residual shrinkage of from 1 to 1 1/2%, but that shrinkage such as was discovered in these samples "would lead to improper fit, improper length and dimensions of the garment and of course, it would make a garment unsatisfactory." (Tr. 110.) He further testified that a fabric would have to be treated or stabilized to obtain residual shrinkage of only 1 to 1 1/2%. Stabilization is an additional costly process which can be undertaken by either the manufacturer or purchaser of the fabric. A claim of 1 to 1 1/2% residual shrinkage by the manufacturer would lead the purchaser to believe that the stabilization process had already been performed on the fabric (Tr. 195) and therefore to pay the higher price obtainable for stabilized fabrics. (Tr. 196.) [23]

Relief Factors

38. *Previous Assurances.* Signor Banci and his American corporate instrumentalities are not strangers to charges of fabric misbranding. A prior proceeding before this Commission, begun in 1961 and terminated in 1971, resulted in a dismissal of misbranding charges involving some rather close questions, on the condition that respondents Banci and Verrazzano "endeavor to engage in cooperative compliance procedures with the Commission's staff." *Verrazzano Trading Corporation t/a Lan Etruria, et al.,* 78 F.T.C. 637, 674-675 (1971). While complaint counsel made no effort to prove noncooperation in compliance procedures, as such, our findings of substantial misbranding during 1973-74 now leave no doubt that respondents were not cooperating and indeed cast considerable doubt on the good faith of respondents when they pleaded in the prior case that they were "anxious to avoid future difficulties under the Textile Act as well as the Wool Act" and would "cooperate in a voluntary enforcement procedure. . ." *Ibid.,* p. 666.

39. *Warnings and Complaints.* Beginning in December 1972 (prior to this Commission's 1973-74 testing program) respondents admittedly received a substantial number of notifications from U.S. Customs that their shipments of wool and/or textile products had not been labeled in accordance with the Wool Act and/or the Textile Act. (RA I, ¶ 599.) Indeed, respondents' counsel conceded: "He (Banci) was receiving the notices (concerning fiber content) from Customs almost daily. . . . Not daily notices but you (Complaint

Counsel) know very well that . . . Customs frequently gave him notices and I have to admit that because its true" (and) "you should have copies. . . ." (Tr. 45–46.) As respects residual shrinkage, complaints were made to respondents by at least two customers, Starward and Bobbie Brooks. (Tr. 44.) [24]

40. *Abandonment of Practices.* Respondents rely heavily on Customs reports of four 1976 fabric test results turned over to respondents by complaint counsel before the hearing. (RX 7–10.) These reports tend to show no misbranding of primary textile constituents substantially in excess of 3% except for a fairly slight overstatement of one constituent (-4.5%) in one of the four tests (RX 8). Respondents concede that evidence of little or no misbranding in 1976 would not be a defense to a charge of misbranding in 1973–74 (Tr. 295–6) but argue that it could be taken into account in determining the terms of the order (Tr. 296). Complaint counsel, for their part, did not seriously question the accuracy of the four reports, arguing principally that four tests were much too few on which to base sweeping conclusions about all of respondents' 1976 importations (Tr. 294–5, 328). We admitted the test results but with a caveat that little weight might be attached to them. (Tr. 328.) Mature reflection has not changed our initial reaction. We find that the four reports (RX 7–10) accurately report what they purport to show but in the absence of further proof, which respondents did not even attempt, we decline to draw therefrom any inference as to whether these few tests fairly represent a substantial quantity of respondents' 1976 importations.

41. *Abandonment of Respondents' Business.* There have been occasional unsworn assertions by respondents' counsel to the effect that the Banci enterprise was in serious trouble. Thus, at a prehearing conference on 11/16/76, respondents' counsel stated (at Tr. 74–5):

> The financial situation in Italy is atrocious. Mr. Banci informs me that he is owed substantial monies by the government of Italy. He is not receiving them. I've mentioned before (that) he hasn't been paying my firm for what we've done. [25]
>
> * * * * * * *
>
> Mr. Banci is a very depressed man. . . . and a man who really was the most optimistic of all my clients in the past sounded terrible to me. It was just not the Walter Banci I knew. He wrote me a letter: ". . . . For us the firms Lima Textiles, Inc., Francesco Datini, Inc. and Verrazzano Trading Corporation are dead. And if they are not yet, then we are ready to close them definitely. . . ."
>
> * * * * * * *

Judge Teetor: Counsel, is that list of companies that you read the total list of respondents? Does that cover everybody that is a respondent here?

Ms. Braun: No, there was also listed Lanificio Tuscania, Inc. and Hudson Textile Corporation and Walter Banci.

Mr. Botwinik: I'm certain (that) if Mr. Banci had thought of them he would have included them in the letter because they are dead to all practical purposes. Mr. Banci hasn't been in the United States for, I'd say, three years. I don't know what he is doing. Ms. Braun and Ms. Zweibel told me before (that) there had been a shipment from (in?) September in (from?) his factory. I know he is not shipping in the same quantities he did in the past and any shipments now would be in very small amounts.

42. To such assertions has now been added another unsworn allegation by respondents' counsel in his "Proposed Findings, etc." that Signor Banci's manufacturing company, Lanificio Walter Banci s.a.s. on 9/2/77 was adjudicated bankrupt, with creditors' claims exceeding 14 billion lire (about 17 million dollars). Thus, counsel argue, "it is highly [26] doubtful that Lanificio Walter Banci s.a.s. or Walter Banci, who was the unlimited partner, ... will ever again be involved in the United States fabric trade in any substantial way." (RPF, pp. 1-2.) On this theory, respondents seek to have all findings of fact rephrased from the present to the past tense.

43. Complaint counsel concede that the corporate respondents are "currently dormant" (CCR, p. 10) but note that there is no record evidence that they have ever been dissolved. (CCR, p. 11.) Nor is there record evidence that Walter Banci or the corporate respondents have ceased doing business in the United States or, for that matter, that the Italian partnership, Lanificio Walter Banci s.a.s. is really bankrupt and, if so, under what conditions. *Ibid.* Indeed, it appears that respondents might have some difficulty in attempting to prove cesser of importation, since complaint counsel attach as Exhibit A to their reply to respondents' proposed findings Customs documents which purport on their face to be an exporter's invoice and consumption entry for a textile importation by Lanificio Walter Banci s.a.s. as late as 9/29/77. Obviously, we place no reliance whatever on either party's unverified assertions.

44. The Customs documents, however, may explain why respondents have never attempted to make actual proof of cesser of importation. There being nothing but a little lawyers' rhetoric on which to base a claim of abandonment or discontinuance of the business here, we find no satisfactory evidence that Lanificio Walter Banci s.a.s. is now out of business and no satisfactory evidence that its trade in the United States, though "dormant," may not be revived, either through the corporate respondents or other vehicles. [27]

IV

CONCLUSIONS OF LAW

1. The Federal Trade Commission has jurisdiction over the subject matter of this proceeding and over all respondents.

> *Comment:* Jurisdiction over the subject matter here is found in Section 5 of the Federal Trade Commission Act (hereafter "FTC Act"), 15 U.S.C. 41, et seq.; Section 7 of the Textile Fiber Products Identification Act (hereafter "the Textile Act"), 15 U.S.C. 70e; and Section 6 of the Wool Products Labeling Act (hereafter "the Wool Act"), 15 U.S.C. 68d. Jurisdiction over the person of the five original respondents (Verrazzano Trading Corporation, Francesco Datini Inc., Lanificio Tuscania Inc., Lima Textiles Inc., and Walter Banci) was obtained by delivering a copy of this complaint for each at their place of business at 2 Penn Plaza, New York, New York, on 7/23/75, and by the subsequent general appearance of each by his attorneys, Pavia & Harcourt (for details of which see Procedural History, App. I, pp. i-ii). Jurisdiction over the sixth respondent (Hudson Textile Corporation) was obtained by serving an order amending the complaint to include Hudson on its attorney, Pavia & Harcourt, on 2/18/76 and by said attorney's subsequent general appearance for said respondent (for details of which see Procedural History, App. I, p. v.).

2. The acts and practices charged in the complaint and proved here took place in commerce within the meaning of Section 2(k) of the Textile Act, 15 U.S.C. 70; Section 2(h) of the Wool Act, 15 U.S.C. 68; and Section 4 of the FTC Act, 15 U.S.C. 44. [28]

> *Comment:* All respondents except Hudson concede this. See all answers to complaint paragraph except Hudson's. For our finding of fact that Hudson, as part of a unified family business operation, was necessarily engaged "in commerce" for present purposes, see Finding of Fact # 12.

3. All respondents have constituted a unified family business operation designed to import and sell in the United States wool and textile products manufactured in Italy by Lanificio Walter Banci s.a.s. a partnership between respondent Banci and his wife. Respondent Banci formulates, directs and controls the acts and practices of both the Italian manufacturing partnership and the

American corporate respondents, including the acts and practices that are the subject of this complaint.

> *Comment:* All respondents, including Banci himself, concede the existence of this unified family business operation, Banci's dominance therein and his responsibility for any particular acts and practices challenged here. Findings of Fact # 5 and # 6. For a holding that such dominance of corporate affairs will be enough to hold an individual, see *Tractor Training Service, Inc.* v. *F.T.C.*, 227 F.2d 420 (9th Cir., 1955). Other courts require an additional showing of actual participation in the challenged practices, *Coro, Inc., et al.* v. *FTC*, 338 F.2d 149, 154 (1st Cir., 1964, *cert. den.*, 380 U.S. 954, but that, too, is conceded here. *Ibid.*

4. Respondents have violated Sections 4(a), 4(b) and 9 of the Textile Act, 15 U.S.C. 70b, and 70g, (and thereby also Section 5(a) of the FTC Act, 15 U.S.C. 45) by importing into the United States and selling in interstate commerce substantial amounts of non-wool textile fiber products in which one or more constituents were overstated on the label or other identification device contemplated by the Textile Act. [29]

> *Comment:* Finding of Fact # 28 establishes that respondents have made 29 overstatements of fiber content in Group I of the textiles sampled and listed in Appendix II (not including 8 other overstatements of less than 3 percentage points). Two thirds of these overstatements are there shown to exceed 10 percentage points and a quarter of them to exceed 20 percentage points. Unless respondents' criticism of the Commission's testing methodology has some merit, it seems plain and we find that Group I of Appendix II evidences some 29 clear violations by respondents of the Textile Act (and, by derivation, the FTC Act) during the period 1973-74.
>
> In addition, respondents failed to list all constituent fibers which amounted to over 5% of the total fiber weight on three of the Group I samples tested. (Finding of Fact # 29.1.) By this omission, respondents violated the clear requirements of Section 4(b)(1) of the Textile Act.

Test Methodology

Respondents argue that neither the Textile Act nor the Wool Act nor any regulation under either establishes any particular method for testing the fiber or wool content of specific samples of fabric. They contend (RPF, p. 5) that, absent such statutory standards, complaint counsel must establish the superiority of their tests over all others in order to sustain reliance on them.

Prior Commission cases hold, however, that to support the validity of a test result, it is sufficient that complaint counsel establish only the expertise of the testers and their adherence to general procedures accepted by the scientific community.[13] *Hunter Mills* [30] *Corp.* v. *F.T.C.*, 284 F.2d 70 (2nd Cir., 1960), *cert. den.*, 366 U.S. 903. Such expertise and acceptable methodology were clearly established here. See Findings of Fact # 19-24.1.

A similar question was raised in *Allenton Mills, Inc.*, 60 F.T.C. 1630 (1962). In the initial decision, (which was adopted by the Commission) it was found that the testimony of an expert witness as to the approximate percentages of reprocessed wool in the samples of fabric manufactured by the respondents, constituted "substantial and reliable proof" that said samples contained at least the amounts of reprocessed fibers to which the expert testified. It was further stated therein that:

> [i]t is not essential that a test be capable of determining quantitatively the precise amount of a particular fiber. It is sufficient that the test under proper conditions when undertaken by a qualified expert, determines the approximate amount within reasonable limits. (p. 1640).

In the present case the expert witnesses clearly testified and we have found that their qualifications and the test methodology they employed were acceptable and proper. See Findings # 19-24.1. Although respondents' counsel cross-examined all complaint counsel's experts extensively, he made no serious inroads on their testimony. Moreover, respondents introduced no witnesses of their own to rebut the testimony of complaint counsel's experts. Nor did respondents offer any evidence of tests made by themselves or others which would support the fiber content claims made on their labels and other fiber identification devices.

The 2nd Circuit Court of Appeals' *per curiam* opinion in *Hunter Mills Corp.*, 284 F.2d 70, 71 (2nd Cir., 1960) is dispositive of respondents' contentions in this area:

> The variance in testing techniques between the two experts testifying for the Commission does not impeach the testimony of either. The Commission has the duty of passing on the qualifications of the experts who testify [31] before it, and it may decide that both procedures are proper. . . . Moreover, it is unlikely that the allegedly "proper" procedure would have changed the ultimate fact-finding, since the percentages of wool content were substantially below those permitted by statute.

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[13] Respondents' citation of the Flammable Fabrics Act, 15 U.S.C. 1191, and the United States Grain Act, 7 U.S.C. 71, as statutes which provide specific test procedures to be followed seems to us to cut the other way. They show that if Congress wanted a specific test procedure followed, Congress would have said so.

We conclude that there is nothing to respondents' attack on the testing process employed here.

Understatements of Fiber Content

Finding of Fact # 29 establishes that in addition to the 29 *overstatements* of fiber content analysed in Finding # 28 there were also 38 substantial *understatements* of fiber content in Group I. As to whether these should be held violations of the Textile Act in the present confused state of the law we are uncertain. In the predecessor case, *Verrazzano Trading Corporation, t/a Lan Etruria, et al.,* 78 F.T.C. 637, 670–71 (1971), this Commission expressly disagreed with but followed, as *stare decisis,* the ruling of the Second Circuit Court of Appeals in *Marcus* v. *Federal Trade Commission,* 354 F.2d 85 (2nd Cir., 1965) that an *understatement* of wool fiber content is not misbranding within the meaning of the Wool Act. Since the same logic seems applicable to understatements of *non-wool textiles,* we are inclined to apply the same rule here. Accordingly, we conclude that respondents did not, by *understating* certain fibers as shown in Finding # 29 add to the violations of law resulting from their *overstating* fiber content, as shown in Finding of Fact # 28.

5. Respondents have violated Sections 3, 4 and 8 of the Wool Act, 15 U.S.C. 68a, 68b and 68f (and thereby also Section 5(a) of the FTC Act, 15 U.S.C. 45) by importing into the United States and selling in interstate commerce substantial amounts of wool products in which the wool fiber content was overstated on the label or other identification device contemplated by the Wool Act. [32]

> *Comment:* Finding of Fact # 31 establishes 25 instances where respondents overstated the wool content of their textiles, in 23 of which instances the overstatement was between 10 and 20 percentage points. Assuming, as we do, that respondents' attack on the Commission's testing methodology is no more convincing with regard to wool than with regard to other textile fibers, we conclude that the textile samples of Group II of Appendix II evidence some 25 clear violations by respondents of the Wool Act (and, by derivation, the FTC Act) during the period 1973–74.
>
> In addition, respondents failed to list all constituent fibers which amounted to over 5% of the total fiber weight on twenty-one of the Group II samples tested. (Finding of Fact # 33.1.) By this omission, respondents violated the clear requirements of Section 4(2)(A) of the Wool Act.

Effect of Wool on Misbranding of Other Textiles

Finding of Fact # 32 establishes that wool was not the only fiber overstated in Group II textiles. It shows 29 overstatements of non-wool fibers considerably in excess of the Commission's "tolerance" (3%). A question naturally arises as to why 29 substantial overstatements of other textile fibers should not be actionable without regard to whether they occur in fabrics which contain wool.

The theory of non-actionability turns on Section 2 of the Wool Act, which makes a fabric containing any wool a "wool product" and Section 2 of the Textile Act, which exempts "wool products" from the strictures of the Textile Act. Against all common sense, therefore, all other textile fibers in a fabric that contains wool escape the requirements of *either* the Wool or Textile Acts. And this Commission in the earlier *Verrazzano* case, at pp. 670–1, apparently accepted such conclusion as the inevitable result of the Second Circuit's *Marcus* opinion (*supra*, pp. 670–1). [33]

Accordingly, we feel bound to hold that the overstatements of non-wool fiber content marshaled in Finding of Fact # 32 do not add anything to our finding of 25 misbranding violations arising out of overstatements of the wool content of Group II textile samples.

With reference to the *understatements* marshaled in Finding of Fact # 33, we are governed by the same considerations set out in connection with Group I textile samples (p. 31, above).

6. Respondents have violated Section 5(a) of the FTC Act, 15 U.S.C. 45, by engaging in certain unfair and deceptive acts and practices in the importation of wool and other textile products into the United States and the sale of substantial quantities of such textiles in commerce.

> *Comment:* Insofar as the complaint charges violations of the FTC Act as simple derivatives of violation of the Wool and Textile Acts (see Section 3 of both Acts), we have already noted that failure to prove the Wool or Textile Act charge automatically carries with it failure of the derivative FTC Act charge. When, however, an independent FTC Act charge is pleaded, the situation is different: the question then is simply whether all the essential elements of an unfair/deceptive practice case have been made out.
>
> Here Section 5(a) of the FTC Act has been invoked to reach several situations where it was apparently felt that neither the Wool nor the Textile Act could reach the wrong. One includes the Group III textile samples (see Findings of Fact # 34–35) where, for reasons already explained, the wool contents are marginal (averaging only 3.5% of total fiber weight), yet by their

presence make it impossible in the existing confused state of the law to reach 16 serious overstatements of other (non-wool) fibers in these "wool products." [34]

A second situation where Section 5(a) of the FTC Act is invoked is found in the wool products exhibits of Group II (CX 4, 19-28, 31-33 and 35-45). The respondents admitted that their sales invoices for these wool products contained the same representations of fiber content as the product's other labels and tags. (RA I, ¶ 26; RA III, ¶ 33 through ¶ 37.) We have already found substantial deviations between fiber content as represented by respondents and actual tested fiber content. (Finding # 31.) However, the Wool Act, unlike the Textile Act, does not reach misrepresentations made on sale *invoices.* (cf. § 4(a) of the Textile Act, § 4(a)(1) of the Wool Act). Therefore, complaint counsel hope to invoke Section 5(a) of the FTC Act, arguing that "the gross misrepresentations to customers made by respondents on the sales invoices relating to these misbranded wool products are false and deceptive acts or practices under the Federal Trade Commission Act." (CPF, p. 42.)

A third such situation is set out in our Findings of Fact # 36-37 on misrepresentations by respondents to their customers regarding residual shrinkage, which are not, of course, governed by misbranding laws.

In all of these situations the threshold question is: what does proof of an unfair method of competition and/or deceptive act or practice entail that is not required to establish a Wool Act or Textile Act violation? More specifically, is the deceptive capacity or tendency which is the bare minimum for a Section 5 violation sufficiently evidenced by the mere fact of misbranding or must something more be shown? [35]

It is well established that proof of a Section 5 violation does not require a showing of actual injury or deception but only a capacity or tendency to injure or deceive. *Charles of the Ritz* v. *Federal Trade Commission,* 143 F.2d 676, 680 (2nd Cir., 1944). Still, there is supposed to be some record evidence as to how consumers may be injured or misled, as to price, quality, etc. *Federal Trade Commission* v. *Winstead Hosiery Co.,* 258 U.S. 483 (1922). That seems to be at least a theoretical difference between such cases and those brought under the Wool or Textile Acts, which "may be violated despite the absence of actual deception or a tendency to deceive. . ." *Taylor-Friedsan Co., Inc., et al.,* 69 F.T.C. 483, 494 (1966).

While we would certainly not be shocked by the idea that deceptive tendency may reasonably be inferred from misbranding alone, we cannot make out that the law has progressed quite that far. Accordingly, we now conclude that neither the misbranding of Group III textile samples nor the misbranding of a textile product on a commercial invoice is sufficient, standing alone, to prove the deceptive tendency requisite to a Section 5 FTC violation. On the other hand, the charge of misrepresentation regarding residual shrinkage is supported here by sufficient additional evidence of deceptive tendency, as developed in Findings of Fact # 36–37, to justify a conclusion that Section 5(a) of the FTC Act has been violated independently in that respect and we now so conclude.

V

RELIEF

The "Public Interest" Defenses

Respondents have made several arguments as to why their violations of the Wool Labeling and Textile Fiber Identification Acts, even if established, should not be made the subject of an order by this Commission. [36] All such arguments are based ultimately on the rule laid down by Justice Brandeis in *Federal Trade Commission* v. *Klesner,* 280 U.S. 19 (1929). That case held that when the facts established in a proceeding before the Commission show, as a matter of law, that the relief would not be in the public interest, the complaint should be dismissed. Whether this holding in an FTC Act case has any application to special statutes enforced by the Commission seems very doubtful but for present purposes we assume, *arguendo,* such applicability.

The *Klesner* rule, although understandably popular among respondents, has not had the wide-ranging application that its statement might suggest. As a practical matter, it has been substantially confined to three kinds of situations which are, in fact, the ones relied upon by respondents here.

1. Private vs. public interest

In *Klesner* the unfair method of competition involved was the appropriation of a competitor's trade name in the retail window shade business in Washington. The Supreme Court, affirming dismissal of the suit, said:

> To justify filing a complaint the public interest must be specific and substantial.

* * * * * * *

> The undisputed facts, established before the Commission at the hearings on the complaint showed affirmatively the private character of the controversy.

This aspect of the *Klesner* decision is now codified in Commission Rule 2.3:

> The Commission acts only in the public interest and does not initiate an investigation or take other action when the alleged violation of law is merely a matter of private controversy and does not tend adversely to affect the public.

[37] While a purely private dispute is thus beyond the purview of the Federal Trade Commission it is nevertheless equally clear from these statements of the law that a dispute affecting the public interest is not beyond the Commission's jurisdiction merely because a private interest, as commonly happens, is *also* involved. For that reason while Klesner's language concerning private controversies has sometimes been quoted in other cases, the "rule" itself has rarely been deemed appropriate for application to particular factual situations. See, for example, *Curtis Publishing Company,* 78 F.T.C. 1472 (1971), where the hearing examiner held that a complaint seeking refunds for subscribers after the Saturday Evening Post suspended publication involved only a private controversy and should be dismissed but the Commission reversed, holding that the vindication of private rights was merely incidental to the proceeding's main purpose to terminate an illegal practice and cure its effects.

Respondents argue here (RPF, p. 8) that the question whether the shrinkage characteristic of fabrics sold by respondents was misrepresented is "solely between Bobbie Brooks and (respondent) Banci and not within the scope of the Act." Citing *Klesner* and noting that the Brooks-Banci dispute has already been the subject of court proceedings to determine the merits of the claim, respondents argue: "For the Commission to interpose itself in this matter and use it in the present matter (manner?) smacks of a persecutional (sic) approach." (RPF, p. 8.)

Although the samples introduced in support of the shrinkage allegation of the complaint happen to have come from Bobbie Brooks, the record shows that substantial quantities of the affected qualities (Sioux and Totem) were sold to United States customers (Finding of Fact # 8). Bobbie Brooks was not the only customer to complain on this score. (Tr. 44.) Misrepresentations of the shrinkage characteristic of these qualities constituted an unfair and [38] deceptive practice injurious to all buyers and to the public in general, not merely to the particular buyer whose evidence happened to prove the allegation. The existence of Bobbie Brooks' private interest in this matter is by no means inconsistent with the existence of a public interest in putting an end to the practice.

2. *De minimis* argument

The *Klesner* rule has sometimes been invoked when the violation proven is claimed to have affected only a inconsequential volume of business. A classic *de minimis* case was *Matter of William S. La Rue*, 47 F.T.C. 1472 (1950). There the Commission affirmed a hearing examiner's order of dismissal where a Chicago barber, without factory, laboratory or any employees made and sold his patrons about a thousand dollars worth of hair tonic over a year's period. Despite undisputed evidence that his claims for this concoction were exaggerated or untrue and therefore misleading and deceptive, it was held that such "inconsequential" volume would not support an allegation of substantial amount of commerce and that further proceedings would not be "in the public interest."

Once we move beyond obvious trivia, however, the Commission has been reluctant to disregard violations just because they are slight and the courts have properly been reluctant to interfere with the Commission's exercise of discretion in this respect. Thus the 2nd Circuit Court of Appeals pointed out in *Exposition Press Inc.* v. *FTC*, 295 F.2d 869 (2d Cir., 1961), a "vanity press" deception proceeding, that even though a particular case may seem trivial it may be "the means whereby in the long run the Commission may use its influence to prevent continuance of many similar deceptions." (p. 873.) Another appellate court has pointed out that the whole purpose of the Federal Trade Commission's policing of business practices is to prevent the growth of unfair acts and practices by stopping them, wherever possible, in their incipiency. This [39] purpose, by its very nature, will not infrequently result in the bringing of cases which may seem insignificant but are not. *Guziak* v. *F.T.C.*, 361 F.2d 700 (8th Cir., 1966); *cert. den.*, 385 U.S. 1007. (Deceptive practices by seller of aluminum siding held properly forbidden.) Indeed, to put it broadly, not even a mere tendency to deception — as distinguished from actual deception — is too trivial for Commission attention. *Spiegel, Inc.* v. *FTC*, 494 F.2d 59, 62 (7th Cir., 1974).

In this case respondents' *de minimis* claim goes neither to the volume of business involved, as claimed in *Surf Sales Co., Inc.*, 54 F.T.C. 483, 491-2 (1957), nor to the infrequency of violations, as claimed in *Hoving Corporation* v. *F.T.C.*, 290 F.2d 803 (2d Cir., 1961) but to the extent of deviation from the wool/fiber content represented by the seller on invoices, consignee declarations, labels, etc.: "Even if the Commission's results (test) were accurate, the margin of error is so slight that we may well question the harshness of the remedies demanded." (RPF, p. 9.) Similarly, respondents' tests are said to "show a variation so slight as to render the order sought by complaint counsel overly harsh and punitive." (RPF, p. 10.)

It is plain, however, that we are not here dealing with "slight" (or even borderline) variations from represented wool/fiber content. No reasonable person could so describe the 29 substantial violations of the Textile Act summarized in Finding of Fact # 28 and the 25 additional substantial violations of the Wool Act summarized in Finding of Fact # 31. This is not a *de minimis* case.

3. Abandonment argument

The third area where *Klesner* has frequently been invoked is the claim of discontinuance or abandonment of either the practice charged or the business itself. Since the purpose of a cease and desist order (and presumably of a [40] compliance bond, too) is therapeutic rather than punitive, the need for an order to protect the public has long been thought to disappear if there is no reasonable expectation that the violation proved will likely be repeated.[14] *Stokely-Van Camp, Inc.* v. *FTC*, 246 F.2d 458, 464–5 (7th Cir., 1957). While, however, the abandonment defense is well recognized and frequently pleaded by respondents, it is equally clear that not every disclaimer of intent to continue the practice or the business itself will move the Commission to dismiss a case on public interest grounds.

Thus the abandonment should be voluntary and that normally means before the Commission's hand is on the respondent's shoulder. *Spiegel, Inc.*, 86 F.T.C. 425, 446 (1975). It also normally means an abandonment of some duration, although not necessarily the decade or so understandably held to justify dismissal of charges in *New Standard Publishing Co.* v. *F.T.C.*, 194 F.2d 181 (4th Cir., 1952). In sum, what is called for is assurance that an alleged abandonment is in good faith and that there is no real likelihood of resumption of an unfair/deceptive practice after the threat of legal action has disappeared. *Beneficial Corp., et al.*, 86 F.T.C. 119, 165 (1975). "And the Commission has required respondents to meet a heavy burden to prevail on such a claim." *Ibid.*

Our Findings of Fact # 40 – # 44 make it clear that while the corporate respondents may recently have been "dormant," there is no good proof in this record that Signor Banci, the dominant figure in this "unified family business organization," is [41] out of business and certainly no proof that he may not resume his American operations through the corporate respondents or other vehicles when this proceeding is over. To forego a proper order on the basis of unsworn and doubtful speculations by counsel as to possible abandonment of the business would be an error of the first magnitude. We reject any such suggestion.

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[14] Although this case does not involve a possible redress suit, it should be noted that there is real doubt since passage of the Magnuson-Moss Act, 15 U.S.C. 2301 in 1975 as to whether the public interest will ever permit dismissal of a cease and desist proceeding, if redress is a purpose of the proceeding.

The administrative law judge concludes that the violations of the Wool Act, Textile Act and FTC Act heretofore found to exist are all to the prejudice and injury of the public and that the relief hereafter ordered is in the public interest.

The Penal Bond

Respondents lay great stress on the prayer of the complaint that they be prohibited from further importing or participating in the importation of any wool or textile products unless they post a bond under Section 8 of the Wool Products Labeling Act and Section 9 of the Textile Fiber Products Identification Act, in double the value of any imports, conditioned on respondents' compliance with all applicable provisions of the above Acts and regulations thereunder. Respondents assume that such a bond is essentially a penal bond rather than an indemnity bond and we are inclined to agree with that assumption.[15]

From this starting point, however, respondents concoct a complex and confused argument with most of which we cannot agree. We now attempt to analyze what appear to be the high points of this argument. [42]

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[15] Since the statute of 8 and 9 William III, cap. 11 (1696–97), (the gist of which is now found in 28 U.S. 1874), Anglo-American law courts have been authorized, like equity before the statute, to assess only actual damages for breach of a penal bond, unless the difficulty of determining actual damages justified the parties in recourse of a liquidated damage clause. For a classic dispute between *private* parties over whether a particular contractual stipulation should be treated as a penalty or as an agreed ascertainment of damages, see *Sun Printing & Publishing Association* v. *Moore*, 183 U.S. 642, 662–3 (1902) (penalty enforced.) However, in the case of penalties or forfeitures to the government imposed by statute upon the doing or omission of a certain act, there courts will not generally interfere to mitigate the penalty or forfeiture, if incurred, for it would be in contravention of the direct expression of the legislative will. *Clark* v. *Barnard*, 108 U.S. 436, 457 (1883) (penalty enforced.) [This case contains an excellent discussion of the history of the problem, at pages 454–456.]

An illustration of the usual result when a statutory bond is in question (penalty enforced) is found in *U.S.* v. *Dieckerhoff*, 202 U.S. 302 (1906). This case involved an importer's re-delivery bond for double the value of certain imported packages released to him during tests of a sample package: "In our opinion, it was the purpose of this statute and the bond executed in the case, to dispense with the necessity of resort to . . . showing damages and to fix double the value of the package ordered to be returned, as a definite sum to be paid for now fulfillment of the statutory duty. In such cases the recovery is for the stipulated sum and is not limited to the damages actually proven" (p. 311). While there are cases where a penal bond payable to a government has been held mere security for indemnification against proven damages, such cases require a very clear showing of intent to invoke an indemnity bond, not a penal bond. See, for example, *U.S.* v. *Zerby*, 271 U.S. 332, 339 (1926), where as here, the bond was conditioned on compliance with all applicable laws and regulations. However, the administrative history there left no doubt that the government's own interpretation of the bond had always been that the penal sum was only a ceiling on all obligations incurred by breach of the compliance bond.

Respondents' own summary of their thesis is as follows:

> Imposition of a penal bond on the facts of this case represents a criminal sanction and consequently should not be imposed under the guise of a civil enforcement proceeding. (RPF, p. 10.)

This cavalier assimilation of the penal bond contemplated in Sections 8 and 9 of the Wool Labeling Act and Textile Fiber Identification Act with the criminal penalty provisions of Sections 10 and 11 of the same statutes is insupportable. While there is some overlap, the concepts of "penalty" and "fine" do not necessarily have the same meaning. [43]

> In general a fine is a sum of money exacted of a person guilty of a crime or contempt as a pecuniary punishment, the amount of which may be fixed by law or left to the directions of the court. It is true that a penalty, like a fine, is a pecuniary punishment inflicted by the law for its violations, *but a penalty is that which is demanded for the violation of a statute, which violations may or may not be a crime.* Indeed, statutes giving a penalty for committing a prohibited act [sometimes] preserve the distinctions by providing that the penalty may be recovered in a civil action, while the crime, if it be so declared, must be punished by the infliction of a fine or imprisonment, after a conviction in a criminal action. 36 Am. Jur. 2d, *Forfeiture and Penalties,* § 4 (emphasis and bracketed matter added)

Thus the U.S. Supreme Court has affirmed a holding that where a state constitution set apart as a permanent literary fund all "fines" collected for offense committed against the state, such provision comprehended only those fines which were affixed as penalties for *crime* and recoverable on the convictions of the offender but did *not* embrace those pecuniary penalties provided by statute that a popular or *qui tam* action ("which is a civil action") might be brought to recover. *Southern Exp. Co.* v. *Commonwealth (of Virginia), ex rel. Walker,* 92 Va. 59, 22 S.E. 809 (1895); *aff'd,* 168 U.S. 705 (1897). Here the penalty bonds in question are [44] found in sections which make no reference to criminal penalties and are entirely separate from those sections (9 and 10) headed "Criminal Penalty." Accordingly, there is no basis on which to treat the penal bonds as the "equivalent" of criminal sanctions.

Although the logic of respondents' argument is extremely difficult if not impossible to follow, they apparently argue that if a penal bond may be assumed to be the "equivalent" of a criminal sanction,

> . . . the principles underlying the section dealing with criminal sanctions must be applied to the provision for posting of bonds by an importer, in order to insure equitable and just enforcement of the laws. (RPF, p. 14.)

While this is an interesting jurisprudential speculation, it flies on the face of several hundred years of Anglo-American law, which has never required that the plaintiff in a *qui tam* or other civil penalty action must prove his case beyond a reasonable doubt or satisfy other of the more strigent requirements of a criminal trial. (One good reason, of course, is that the defendant in a civil penalty action is not faced with the possibility of imprisonment as a sanction, if he loses.)

The ultimate goal of respondents' tortured logic seems to be the preposition that if a civil penalty could be viewed as the "equivalent" of a criminal sanction, the civil penalty provision concerned here would not be constitutional unless construed to apply only to "willful or intentional misconduct as the term is understood in the criminal law" because "(t)he fundamental distinction between a criminal versus a statutory violation of either Act is the element of willful or intentional misconduct, as the term is understood in the criminal law." (RPF, p. 15.) It should be sufficient to point out that while a *mens rea* is still generally required in a case of *mala in se*, for *mala prohibita* there is no requirement of a *mens rea*, especially in the area of public welfare offenses. These are crimes which depend on no mental element but consist only of forbidden acts or omissions. *Morisette* v. *United States*, 342 U.S. 246 (1952). Where [45] the legislature creates such an offense, criminal intent in any of its forms — including "wilfulness" — is no element of the crime and need not be proved to justify a conviction, *People* v. *McClennegen*, 195 Cal. 445, 234 P. 91, 100-1 (1925) although some courts reconcile this with the older law of crimes by saying that where a statute denounces the doing of an act as criminal, the law imputes criminal intent from the mere doing of the act. *Hargrove* v. *United States*, 67 F.2d 820 (5th Cir., 1933). The only question is whether the prohibited act was done or the required act omitted. *United States* v. *Balint*, 258 U.S. 250 (1922).

> While, in a certain sense, intent is essential to the commission of a crime and in some classes of cases it is necessary to show moral turpitude in order to make out a crime, there is a class of cases where purposely doing a thing prohibited by statute may amount to an offense, although the act does not invoke turpitude or moral wrong. *Armour Packing Co.* v. *United States*, 209 U.S. 56 (1908).

Since a statutory crime need involve no *mens rea*, it follows a fortiori that a statutory *civil penalty* — even if it were viewed as the "equivalent" of a crime — need involve no "wilfulness" or other specific intent to violate the law. Thus there is no reason for reading the word "wilful" into the penal bond clauses of Section 8 of the Wool Products Labeling Act of Section 9 of the Textile Fiber Products Identification Act, as urged by respondents.

A further argument by respondents is that while Congress concededly ("expressly") granted the Commission authority to enforce both the Wool Labeling and Textile Fiber Products Identification Acts, "such jurisdiction is not without limits" (RPF, p. 14). Respondents' brief, at the same page, purports to "quote" a statement attributed to the U.S. Supreme Court in *F.T.C.* v. *Ruberoid Co.,* 343 U.S. 470, 473 (1952) but, in fact completely rewritten by respondents' counsel: [46]

Supreme Court Statement	*Verrazzano Version*
"Orders of the Federal Trade Commission are not intended to impose criminal punishment or exact compensatory damages for past acts, but to prevent illegal practices in the future."	*"Commission proceedings are neither compensatory nor punitive in character, they are strictly corrective and preventive measures taken (in) the interest of the general public."*

The same brief, at p. 17, argues that "in view of the fact that a bond would operate as a punishment for past acts, while the Commission's authority is directed to the regulation of future activities, it is inappropriate to invoke it here."

We note that the requirement of a compliance bond in double the value of respondents' imports serves the very purpose "to prevent illegal practices in the future" stressed by the Supreme Court in *Ruberoid.* However, we need not decide whether such a bond could be justified as part of an ordinary cease and desist order because it is plain that the Supreme Court was speaking in the context of a Clayton Act rather than a Wool Labeling or Textile Fiber Products Act violation. Neither the Clayton nor Federal Trade Commission Acts contains any such penal bond provisions as are found in the Wool Labeling and Textile Fiber Products Identification Acts. In the latter cases, however, Congress explicitly granted this Commission authority to prohibit a proven violator from making further importations without posting a compliance bond. Whether this Commission would have authority to require such a compliance bond if the Wool Labeling and Textile Fiber Products Acts had never been passed is a purely academic question which has no bearing on this matter.

Finally, respondents argue that "if a mere finding that goods have been misbranded by an importer could give rise to the use of a bond, it would be clear that importers were being held to a far higher standard than all other groups who fall within the purview of the Acts." (RPF, p. 11.) The fact that we are dealing here with [47] the importations of foreign goods into this country — and thus dealing frequently with unusual jurisdictional, procedural and executional problems — would seem to justify classification as between those who participate in importation arrangements and have already at least once violated the law, on the one hand, and, on the other, those who may also have violated the law but are engaged only in the more easily policed domestic trade. Consider, for example, the continuing validity of so-called foreign attachment in the face of the present Supreme Court's virtual demolition of domestic attachment/garnishment before judgment under ordinary circumstances. *Cf. Ownbey* v. *Morgan*, 256 U.S. 94, 110-112 (1921) and *Sniadach* v. *Family Finance Corp. of Bay View*, 395 U.S 337, 339 (1969).

We do not, however, propose to involve this tribunal in the constitutional argument which respondents seek to make. We have hitherto already stricken a substantially identical affirmative defense contained in ¶ 5 of the answers of all respondents except Hudson Textile Corporation. See both initial ruling (7/14/76) and denial of applications for review (10/1/76). In the latter we said:

> Since it is elementary law that the constitutionality of Congressional legislation cannot be litigated before this Commission (or, *a fortiori*, before this Administrative Law Judge), Davis K., *Administrative Law Text*, (3rd Ed., 1972)), pp. 388-89, injection of such an issue into the pleading and proof of this proceeding would only confuse the issues and waste time. We do not think there is even a serious doubt about this.

Nothing has since been said by respondents to change our mind. Our ruling declining to consider the constitutionality of a compliance bond for violators involved in importation arrangements remains the law of this case. [48]

Necessity of Imposing a Bond in This Case

To require respondents to post a bond for double the value of their imports is particularly appropriate to their situation. Despite assurances of good intention in 1971, and although since 1972 respondents have received numerous notifications from U.S. Customs advising that their shipments of wool and textile products had not been labeled in accordance with the Wool Act and the Textile Act, (Findings of Fact # 38-9). Respondents, nevertheless, continued to import into the United States misbranded wool and textile products. This evidences a blatant disregard, on respondents' part, of the labeling laws of this country.

Respondent Banci resides in Italy, the corporate respondents are currently dormant and apparently have no assets in the United States. Under these circumstances, liability for civil penalties alone might present no deterrent to future misconduct by respondents as disregarding a Commission cease and desist order may not result in any financial loss. Requiring respondents to post bonds, conditional upon compliance with our labeling laws, is the only way to insure that the respondents will adhere to the mandates of those laws.

The following order will issue:

ORDER

It is ordered, That respondents Verrazzano Trading Corporation, a corporation, Francesco Datini Inc., a corporation, Lanificio Tuscania Inc., a corporation, Lima Textiles Inc., a corporation, and Hudson Textile Corporation, a corporation, their successors and assigns and their officers, and Walter Banci, individually and as agent for said corporations, and as an officer of Lanificio Tuscania Inc. and Lima Textiles Inc., and as a partner trading and doing business as Lanificio Walter Banci s.a.s., and respondents' representatives, agents and employees, directly or through any corporation, subsidiary, division, or any other device, in [49] connection with the introduction, sale, advertising or offering for sale in commerce, or the transportation or causing to be transported in commerce, or the importation into the United States of any textile fiber product; or in connection with the sale, offering for sale, advertising, delivery, transportation, or causing to be transported, of any textile fiber product which has been advertised or offered for sale in commerce; or in connection with the sale, offering for sale, advertising, delivery, transportation or causing to be transported, after shipment in commerce of any textile fiber product, as the terms "commerce" and "textile fiber product" are defined in the Textile Fiber Products Identification Act, do forthwith cease and desist from misbranding such textile fiber products by:

1. Falsely or deceptively stamping, tagging, labeling, invoicing, advertising or otherwise identifying such products as to the name or amount of constituent fibers contained therein.

2. Failing to affix a stamp, tag, label, or other means of identification to each such textile fiber product showing in a clear, legible and conspicuous manner each element of information required to be disclosed by Section 4(b) of the Textile Fiber Products Identification Act. [50]

It is further ordered, That respondents Verrazzano Trading Corporation, a corporation, Francesco Datini Inc., a corporation, Lanificio Tuscania Inc., a corporation, Lima Textiles Inc., a corporation, and Hudson Textile Corporation, a corporation, their successors and assigns and their officers, and Walter Banci, individually and as agent for said corporations and as an officer of Lanificio Tuscania Inc. and Lima Textiles Inc. and as a partner trading and doing business as Lanificio Walter Banci s.a.s., and respondents' representatives, agents and employees, directly or through any corporation, subsidiary, division, or other device, do forthwith cease and desist from importing, or participating in the importation of, any textile fiber product into the United States except upon filing bond with the Secretary of the Treasury in a sum double the value of said products and any duty thereon, conditioned upon compliance with the provisions of the Textile Fiber Products Identification Act.

It is further ordered, That respondents Verrazzano Trading Corporation, a corporation, Francesco Datini Inc., a corporation, Lanificio Tuscania Inc., a corporation, Lima Textiles Inc., a corporation, and Hudson Textile Corporation, a corporation, their successors and assigns and their officers, and Walter Banci, individually and as agent for said corporations and as an officer of Lanificio Tuscania Inc. and Lima Textiles [51] Inc. and as a partner trading and doing business as Lanificio Walter Banci s.a.s., and respondents' representatives, agents and employees, directly or through any corporation, subsidiary, division, or other device, in connection with the introduction into commerce, or the offering for sale, sale, transportation, distribution, delivery for shipment or shipment in commerce of wool products, as "commerce" and "wool product" are defined in the Wool Products Labeling Act of 1939, do forthwith cease and desist from misbranding such products by:

1. Falsely and deceptively stamping, tagging, labeling, or otherwise identifying such products as to the character or amount of the constituent fibers contained therein.
2. Failing to securely affix to or place on each such product a stamp, tag, label or other means of identification showing in a clear and conspicuous manner each element of information required to be disclosed by Section 4(a)(2) of the Wool Products Labeling Act of 1939.

It is further ordered, That respondents Verrazzano Trading Corporation, a corporation, Francesco Datini Inc., a corporation, Lanificio Tuscania Inc., a corporation, Lima Textiles Inc., a corporation, and Hudson Textile Corporation, a corporation, their successors and assigns and their officers, and Walter Banci, individually and as agent for said corporations and as an officer of

Lanificio Tuscania Inc. and Lima Textiles [52] Inc. and as a partner trading and doing business as Lanificio Walter Banci s.a.s., and respondents' representatives, agents and employees, directly or through any corporation, subsidiary, division, or other device, do forthwith cease and desist from importing or participating in the importation of wool products into the United States except upon filing bond with the Secretary of the Treasury in a sum double the value of said wool products and any duty thereon, conditioned upon compliance with the provisions of the Wool Products Labeling Act of 1939.

It is further ordered, That respondents Verrazzano Trading Corporation, a corporation, Francesco Datini Inc., a corporation, Lanificio Tuscania Inc., a corporation, Lima Textiles Inc., a corporation, and Hudson Textile Corporation, a corporation, their successors and assigns and their officers, and Walter Banci, individually and as agent for said corporations and as an officer of Lanificio Tuscania Inc. and Lima Textiles Inc. and as a partner trading and doing business as Lanificio Walter Banci s.a.s., and respondents' representatives, agents and employees, directly or through any corporate or other device, in connection with the importing, advertising, offering for sale, sale or distribution of wool and/or textile products, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from misrepresenting the shrinkage factor of such products on [53] contracts, invoices, shipping memoranda or labels applicable thereto, or in any other manner.

It is further ordered, That respondents deliver a copy of this order by registered mail to each of their customers that purchased qualities Sioux, Manito, Totem, Marnie, Gretel, Isabel, Veruska, Spluga, Eva, Navajo, Ellen, Ingrid or Myla during the period January 1, 1973 to June 24, 1975.

It is further ordered, That the individual respondent named herein promptly notify the Commission of the discontinuance of his present business or employment and his affiliation with a new business or employment. Such notice shall include said respondent's current business address and a statement as to the nature of the business or employment in which he is engaged, as well as a description of his duties and responsibilities.

It is further ordered, That the corporate respondents shall forthwith distribute a copy of this order to each of their operating divisions and/or subsidiaries.

It is further ordered, That the corporate respondents notify the Commission at least thirty (30) days prior to any proposed change in said respondents such as dissolution, assignment, or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporations which may affect compliance obligations arising out of the order. [54]

It is further ordered, That respondents herein shall within sixty (60) days after service upon them of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied with this order.

APPENDIX I

PROCEDURAL HISTORY[1]

On 6/24/75, the date of issuance of this complaint, it was assigned for hearing to Administrative Law Judge Paul R. Teetor, who thereafter conducted all pre-trial and trial proceedings. The notice hearing set for 8/13/75, was postponed indefinitely on 8/4/75 at the request of certain respondents.

On 8/1/75 respondent Francesco Datini, Inc. and "all other Respondents (not identified) who have been properly served" appeared generally by their attorneys, Pavia & Harcourt, and moved for a more definite statement of charges. Simultaneously, respondent Banci appeared specially by his attorneys, Pavia & Harcourt, and requested a determination whether service of process on him had been properly made. On 8/25/75 complaint counsel filed answers to both the request for a more definite statement and the jurisdictional objection.

In response to the request for a more definite statement, on 9/10/75, reciting complaint counsel's representations that they had been unable to obtain all information required during the pre-complaint investigation of this matter, in an "Order For Bill Of Particulars And Discovery In Aid Thereof" the administrative law judge directed complaint counsel to file all their foreseeable discovery requests (whether or not necessary for preparation of a Bill of Particulars) within 21 days and then, as soon as possible after [ii] receipt of a response, to prepare a Bill of Particulars identifying the name, line and style of the goods referred to in complaint Paragraphs 3, 4, 5, 8, 9, 10 and 13 and also the time period involved. Respondents were given until 10 days after service of such Bill of Particulars to file their answers to the complaint.

In response to the jurisdictional objection, on 9/19/75 the administrative law judge held that service on respondents Banci and

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[1] Dates recited here are those on which papers were filed with the Secretary of the Commission, as shown by docket entries, unless the contrary is expressly stated.

Verrazzano Trading Corporation by delivering a copy of the complaint to one Hamm at the New York office of respondent Francesco Datini Inc. was sufficient to obtain jurisdiction over the person of Banci by collateral estoppel, in view of the Commission's litigated finding only four years earlier that respondent Banci and all respondents named here except Lima Textiles, Inc. constitute "a single unified enterprise — an integrated family-owned business — designed to sell in the United States fabrics manufactured by Lanificio Walter Banci" in Italy and that over this business Banci exercises sufficient direction and control to make him accountable individually for the practices of the unified enterprise and each of its parts. *Verrazzano Trading Corporation, t/a Lan Etruria, et al.*, 78 F.T.C. 637, 638 (1971).

On 9/26/75 the administrative law judge gave formal notice to respondents Verrazzano Trading Corporation, Lanificio Tuscania Inc. and Lima Textiles Inc. that they were in default on their obligation to appear and answer these charges and that an initial decision to that effect would be entered under Rule 3.12(c) unless within 10 days after service of this notice a proper appearance be entered and a proper pleading filed. On 10/6/77 respondents Verrazzano Trading Corporation, Lanificio Tuscania Inc., Lima Textiles Inc. and Walter Banci appeared generally in this proceeding and on the same date requested the benefit of our [iii] earlier "Order For Bill Of Particulars And Discovery In Aid Thereof" filed on 9/10/75. (See p. 2 above) This motion was granted by order filed 10/20/75 and the anticipated default simultaneously held cured.

Meanwhile, on 10/10/75 complaint counsel had made an informal "Initial Discovery Request" for a large number of admissions by respondents. On 10/28/75 complaint counsel moved for a time limit on respondents' answers to said informal discovery request. On 10/29 the administrative law judge directed respondents to make return of all responsive documents and/or information requested within 3 weeks from the date of his order or explain in writing, with affidavits, why such return could not be made by that date.

On 11/17/75 all respondents sought a so-called "protective order" limiting discovery to such information as complaint counsel might need to draft a Bill of Particulars but on 12/1/75 complaint counsel opposed such a restriction on their discovery and any extension of time for respondents to produce. On the same date (12/1/75) the administrative law judge reaffirmed that complaint counsel were to get all their foreseeable discovery out of the way at once, holding that there is nothing wrong with post-complaint discovery simply because a complaint has issued. In view, however, of the number of disputes by then arising concerning such discovery, the administrative law judge directed complaint counsel to convert their voluntary requests into subpoena demands and to make certain changes in their specifications appropriate to such conversion. Forty-five days were allowed for a search and an additional 15 days for communication back and forth between the United States and Italy regarding such search.

On 12/11/75 respondents sought additional time for compliance with complaint counsel's subpoenas, so that their search for responsive [iv] documents might be coordinated with a trip to Italy planned by respondents' counsel. Respondents also sought to begin their own discovery before complying with complaint counsel's subpoenas. On 12/12/75 the administrative law judge denied respondents' motion for intervening discovery but granted a delay until 3/15/76 for return of all requested documents available only in Italy or elsewhere outside the United States. Meanwhile respondents and their counsel were warned that they would be held strictly accountable for the integrity and safe-keeping of all records in this country responsive either to complaint counsel's informal discovery requests or to their new subpoenas, which the adminstrative law judge proceeded to issue on 12/18/75. On 12/19/75 prehearing conferences for the receipt of formal returns were scheduled for 1/22/76 for domestic documents and 3/15/76 for foreign documents.

An informal letter from Pavia & Harcourt, counsel for respondents, dated 12/22/75, informed the administrative law judge that respondent Banci's companies in the United States no longer had any employees here and that counsel could not be held "strictly accountable for the integrity and safe-keeping of these companies' records," although it would "do the best it can" to obtain the "voluminous" and "burdensome" information requested by complaint counsel. On 12/29/75 the administrative law judge by informal letter accepted counsel's assurance that his firm would use its "best efforts" to obtain the requested information but noted the seriousness with which "any substantial loss of relevant records" would be viewed by the administrative law judge.

Pursuant to the aforementioned order filed 12/19/75, a prehearing conference was held in the Commission's Regional Office in New York, N.Y. on 1/22/76 to receive the return of domestic documents called for by complaint counsel's subpoena. [v] No company official appeared to make a return but Mr. Botwinik of Pavia & Harcourt, on his oath of office as an attorney, handed over a few papers he had picked out of his own (attorney's) files. He further suggested that the alleged burden of searching respondents' files here and abroad could be drastically reduced if complaint counsel would submit requests for admissions of the facts to be proved by documents subpoenaed and thereby render production of such documents necessary. The administrative law judge encouraged complaint counsel to submit as many such requests as possible before counsel's forthcoming departure for Europe. Complaint counsel undertook to do so.

On 2/9/76 complaint counsel filed their "Initial Request For Admissions" comprised of 642 proposed factual and documentary admissions. Simultaneously, by letter dated 2/6/76, complaint counsel advised respondent which admissions would render which subpoena calls unnecessary and inoperative. On 3/3/76 complaint counsel filed an additional 170 requests for admissions.

On 2/9/76 complaint counsel moved to amend the complaint by adding as a respondent Hudson Textile Corporation, a New York corporation, alleged to be part of the same unified family business carried on by the original respondents. There being no objection by respondents, said motion was granted by the administrative law judge on 2/10/76. Thereafter Hudson Textile Corporation appeared generally and participated in all proceedings by Pavia & Harcourt, counsel for all respondents.

On 3/22/76 another prehearing conference was held, again in the regional office of this Commission in New York, N.Y. Counsel reported that, with only a few exceptions, the further return of documents in response to complaint counsel's subpoena issued 12/18/75 had now been [vi] rendered unnecessary by respondents' acquiescence in most of counsel's Requests for Admissions. However, with reference to the exceptions (subpoena specifications 13 thru 18), respondents' counsel reported that he had not yet received various responsive documents promised by his clients. Accordingly, the administrative law judge ruled that respondents were now in default and that, unless such default be cured no later than 4/12/76, sanctions would be applied under Rule 3.38.

At the same prehearing conference respondents advised that sufficient knowledge of the case against them had been obtained in the course of complaint counsel's discovery. They accordingly waived their right to the Bill of Particulars granted them by order of 9/10/75. It was then ordered by the administrative law judge that respondents file their answers to the complaint by 4/12/76 and initiate such discovery as they might require no later than 4/26/76, after which complaint counsel would have at least three weeks to respond.

On 4/14/76 three separate answers to the complaint were filed by respondents. Individual respondent Walter Banci admitted the allegations of complaint paragraphs 1, 2, 7 and 12 (except as to his business address); denied all other allegations; and raised five so-called affirmative defenses. A second answer, by respondents Verrazzano Trading Corporation, Francesco Datini Inc., Lanificio Tuscania Inc. and Lima Textiles Inc., made the same admissions and denials of the complaint's allegations (except as to the group's main office and principal place of business) and raised the same five affirmative defenses as respondent Banci's individual answer. The third answer, by lately-joined respondent Hudson Textile Corporation, admitted only the allegations of complaint Paragraph 1 (except those relative to doing business under the laws of New York and relative to its main office and principal place of business) and denied all [vii] other allegations but, unlike the original respondents, raised no affirmative defenses.

On 3/25/76, complaint counsel had filed a motion, under Rule 3.38, for the administrative law judge to make 21 specified findings of fact to compensate for respondents' failure to produce the documents requested in specifications 13 thru 18 of complaint counsel's subpoena duces tecum issued 12/18/75 and, further to preclude respondents from introducing in evidence or otherwise relying in support of any claim or defense upon testimony or evidence relating to any documents responsive to specifications 13 thru 18 and, further, to preclude respondents from objecting to complaint counsel's use of secondary evidence to show what the withheld documents would have shown.

Respondents' answer to this preclusion motion, filed on 4/2/76, asserted (although without benefit of any supporting affidavit) that respondents had submitted "all extant copies" of certain documents sought by the subpoena, attacked the reasonableness of certain of complaint counsel's proposed constructive findings of fact and urged that complaint counsel might better obtain from Customs certain documents sought by complaint counsel as the basis for other proposed findings. By special order of the administrative law judge (4/5/76) complaint counsel were then permitted to reply to respondents' answer. Complaint counsel pointed out (4/8/76) that there had been no testimony or even an affidavit that anyone had searched company files in New York or Italy and that the statements of respondents' counsel were limited to his own legal file. In response to respondents' suggestion that complaint counsel should get the needed documents from Customs, affidavits from Customs officials explained why such would be an "impractical if not impossible task." [viii]

On 4/19/76 the administrative law judge filed his "Application Of

Sanction Under Rule 3.38 For Failure Of Respondents To Make Discovery As Ordered." With respect to proposed findings concerning complaints about shrinkage, it was held that even if statements in court by respondents' counsel on his oath of office should be construed as denying the existence of responsive documents, such "testimony" showed on its face his lack of sufficient testimonial knowledge to make such statements. Complaint counsel's proposed findings # 1 and # 2 were accordingly adopted but subject to a *tempus penitentiae*. Respondents were given five days in which to move for another prehearing conference at which to present the sworn testimony of anyone with actual personal knowledge as to the completeness of whatever search may have been made by respondents and to turn over to complaint counsel all responsive documents found in such search.

No *tempus penitentiae* was allowed, however, with respect to two other deficiencies for which sanctions were sought. Firstly, failure by respondents to produce records responsive to subpoena specifications # 3 thru # 20 was held to be deliberate and willful. Furthermore, their argument that complaint counsel might get the desired evidence from Customs was held legally immaterial and, in any event, an unsatisfactory substitute under the facts here. Accordingly, complaint counsel's proposed findings # 3 thru # 20 were adopted and respondents were also precluded from later offering in evidence any documents which would have been responsive to these subpoena specifications. Secondly, in view of respondents' failure to produce leases, etc. from their files at 2 Penn Plaza in New York, the administrative law judge found that location to be a place of business of respondents in the United States (although declining to infer, as suggested in complaint counsel's proposed finding # 21, it was respondents' "principal" place of business here). [ix]

Finally, a general request for an order precluding respondents from using any evidence which had been denied complaint counsel and, further, permitting complaint counsel to make use of secondary evidence as to such matters was denied for the time being but held in abeyance pending possible application in specific situations.

At another prehearing conference held at the Commission's regional office in New York, N.Y. on 5/4/76 respondents' counsel presented a telex message from respondent Banci reciting a search of Italian files yielding certain stated statistics concerning respondents' volume of business in the United States in 1974 and 1975 but advising that such files yielded no claims by customers concerning the composition of fabrics. Thereupon the administrative law judge ruled that respondents would be relieved of sanctions # 1 and # 2 on receipt of a sworn statement by respondent Banci to the same effect as his telex. After some delays a time limit of 6/11/76 was set for filing such affidavit and after the filing of such an affidavit on 6/14/76, the administrative law judge on 6/22/76 relieved respondents of sanctions # 1 and # 2, while maintaining all other sanctions under the Ruling of 4/16/76 in full force and affect.

At the same prehearing conference (5/4/76) respondents were given five days (later informally extended to seven days) within which to apply for a discovery subpoena and complaint counsel were given five days thereafter to answer the application. On 5/17/76 respondents filed a motion for a broad discovery subpoena and complaint counsel filed their answer on 6/2/76. On 6/23/76 respondents filed a motion for special leave to reply, with proposed reply attached. By this time, however, it had become apparent that the proper scope of respondents' discovery would be greatly affected by the outcome of a pending attack by complaint counsel on respondents' so-called affirmative defenses. [x] Accordingly, no further action on respondents' motion for a discovery subpoena was taken at that time. We turn now to complaint counsel's attack on respondents' affirmative defenses.

On 5/18/76 complaint counsel had moved to strike 4 of 5 affirmative defenses in the answers to the complaint filed by respondent Banci individually and by all corporate respondents except Hudson Textile Corporation. These four affirmative defenses and complaint counsel's position concerning each may be summarized as follows.

Answer § 5

Respondents attacked the constitutionality of the bonding provisions of Section 8 of the Wool Products Labeling Act of 1939 and Section 9 of the Textile Fiber Products Identifications Act (and auxiliary rules and regulations) as denying due process of law and equal protection of the law, because discriminatory in their application solely to importers. Complaint counsel denied that this is a proper forum in which to raise such a constitutional defense and noted that exhaustion of the administrative process might not leave any constitutional question to be decided.

Answer § 6

Respondents asserted that the bringing of this complaint was not really in the public interest because only a private dispute is allegedly involved. Complaint counsel relied upon the principle that once a complaint issues, the Commission's determination that there is a reason to believe a violation has occurred and that a proceeding would be in the public interest are not reviewable. [xi]

Answer § 7

Respondents argued that this is an action designed to protect competitors whereas the purpose of Section 5 of the F.T.C. Act is to protect consumers. Complaint counsel explained that while consumers have been protected explicitly only since the Wheeler-Lea Amendments in 1938, the protection of competitors has always been a purpose of Section 5.

Answer § 8

Respondents' final affirmative defense was that any violations constituted but a small part of respondents' total volume of business. Complaint counsel denied the relevancy of this defense and pointed out that under such a rule a big enough business could violate the law with impunity.

By order filed 5/27/76 respondents were granted until 6/11/76 to answer complaint counsel's motion and on 6/14/76 filed such an answer (see above) elaborating on respondents' position as to each of these four affirmative defenses. On 7/14/76 the administrative law judge filed a lengthy ruling not reaching the merits of the constitutional argument but otherwise granting complaint counsel's motion to strike the affirmative defenses contained in Paragraphs 5, 6, 7 and 8 of the answers of all respondents except Hudson Textile Corporation (whose answer contained no such affirmative defenses).

On 7/20/76 respondents gave oral notice that they intended to apply for interlocutory review of the administrative law judge's decision to strike four affirmative defenses contained in the answers of all respondents except Hudson Textile Corporation. The judge thereupon gave respondents until 8/2/76 to file such application and complaint counsel until 8/16/76 to file any response thereto. The application was filed on 8/3/76 and complaint counsel's reply on 8/12/76. On 10/1/76 the administrative law judge filed another lengthy ruling denying [xii] respondents application for interlocutory review, reaffirming and explaining his earlier opinion as to the impropriety of the four affirmative defenses in question, and finding nothing in his earlier opinion sufficiently doubtful to merit bothering the Commission with a special appeal at this time.

Meanwhile complaint counsel had been seeking a supplementary discovery subpoena said to be required by a fifth affirmative defense

(Par. 4 of all answers to the complaint except that of Hudson Textile Corporation). In a motion filed 8/8/76, complaint counsel recited respondents' pleading that deviations from the stated fiber contents were the result of "unvoidable manufacturing variations despite the exercise of due care. " The interjection of this defense, complaint counsel argued, required discovery which would enable complaint counsel to "trace respondents' manufacturing process from raw material to finished product" in order to determine "at what stage in production unavoidable manufacturing variations may have occurred and what procedures are generally followed at respondent's mill to insure due care and quality control."

On 8/23/76, all respondents moved to limit or quash complaint counsel's requested supplementary subpoena in substantial respects and, in any event, to be given extra time in which to obtain any properly subpoenaed documents from Italy. On 9/1/76 complaint counsel opposed respondents' motion to limit or quash. In his ruling filed 10/1/76 the administrative law judge limited the proposed specifications as requested in certain respects; denied alleged irrelevancy as to one specification; declined to restrict discovery to the time period covered by the complaint; and took the problem of communicating with Italy into consideration in making the revised subpoena returnable at a prehearing conference scheduled for 11/16/76. [xiii]

When said prehearing conference was convened at the Regional Office of this Commission on 11/16/76, respondents' counsel informed the administrative law judge that respondents would neither appear nor produce any of the documents specified in the subpoena duces tecum because of the expense of producing such evidence and because respondents' American business is now relatively insignificant. An oral application in open court by complaint counsel to apply sanctions against respondents under Rule 3.38 for failure to make discovery as ordered was then and there granted by the administrative law judge. It was duly ordered that (1) an inference be drawn that documents responsive to subpoena specifications 1 thru 15 would be adverse to respondents' claim of unavoidable manufacturing variations despite the exercise of due care; (2) it be now established that violations charged in the complaint are not the result of unavoidable manufacturing variations despite the exercise of due care; (3) respondents may not introduce into evidence or otherwise rely, in support of any claim or defense upon any document which would have been responsive to subpoena specifications 1 thru 15; that Paragraph 4 of each of respondents' answers be stricken.

With the pleadings thus pruned, a considerable amount of the discovery sought earlier by respondents now became unnecessary and on the same principle the administrative law judge determined to further postpone his ruling on said discovery request until respondents had received complaint counsel's proposed exhibits and summaries of expected witness' testimony. By order filed 10/1/76 complaint counsel were directed to turn their case over to respondents in two weeks, after which respondents would have another two weeks to revise the specifications of their long-pending requested subpoena duces tecum to eliminate material already received in the turnover. [xiv]

At the aforementioned prehearing conference held on 11/16/76 it was confirmed that respondents would have two weeks (until 11/30/76) to revise the specifications for their discovery subpoena in light of recent developments and complaint counsel would then have four weeks (until 12/31/76) to make responsive production, subject to the usual time limit of 10 days in which to make objections. Thereafter, on 12/10/76 respondents moved for their subpoena duces tecum, specifying eight categories of documents desired from the Commission's files. These included (1) reports on investigations into respondents' textile/wool products; (2) complaints received about respondents' products; (3) communications between the Commission and Bobbie Brooks concerning fiber content or the shrinkage factor of textile/wool products which respondents had sold Bobbie Brooks; (4) studies made by the Commission in connection with the Care Labeling Act; (5) explanations of the manner in which the Commission tests, samples and otherwise enforces the Textile and Wool Acts domestically; (6) statistics comparing the volume of investigations and enforcement proceedings brought against foreign manufacturers and importers with the volume of actions taken against domestic manufacturers and sellers; (7) statistics showing the volume of actions taken under those acts against importers or domestic resellers; and (8) statistics showing the number of field employees enforcing the Textile and Wool Acts, either full-time or part-time. Complaint counsel's opposition was filed on 12/27/76.

On 1/26/77 the administrative law judge denied all of respondents' specifications except (3), as to which complaint counsel were required to produce within two weeks. This ruling was based principally on the view that in most instances respondents were merely "fishing" in the private area of Commission decision-making which is not subject to discovery, absent a showing of probable cause not even attempted here. On the substantive side, it was held, [xv] the Commission's exercise of administrative discretion, as in choosing the sequence of prosecution of different offenders is not ordinarily open to litigation, and mere relevance to the exercise of such discretion is insufficient to make discovery proper in such a situation as this. In view, too, of the striking of respondents' so-called affirmative defenses, all but specification (3) were held improper.

Throughout the pre-trial discovery period a good deal of real progress in preparing for trial was made by the use of many complex admissions requested and accepted under Rule 3.11 (See filings on 9/20/76, 11/1/76, 11/26/76). With the completion of the admissions procedure and reciprocal discovery, as set out above, on 2/11/77 the administrative law judge ordered evidentiary hearings in the New York Regional Office to begin on 3/21/77. He simultaneously ordered respondents to turnover to complaint counsel by 3/4/77 a list of all their proposed exhibits, with copies thereof, and a list of all their proposed witnesses, with summaries of the thrust of their expected testimony. It was further laid down that "witnesses and exhibits not so pre-viewed will not be received in evidence during said hearing." On 3/3/77 complaint counsel were directed to advise respondent of the sequence in which they expected to call their witnesses (the identity and testimony of whom had already been provided to respondent as noted above).

By letter to complaint counsel, with copy to the administrative law judge, respondents on 3/7/77 gave notice that they did not expect to call any witnesses at trial but did submit certain fiber test results and a record of the testimony of one Professor Antonio Rota in an earlier matter (Dkt. 8801) to be offered in this hearing.

Evidentiary hearings began on Monday, March 21, 1977 and continued through Wednesday, March 23, 1977. [xvi]

Complaint counsel called the following witnesses:

Name and Address 1	*Date of Testimony*	1 *Transcript Reference*
Samuel A. Golub 1000 Providence Highway Dedham, Mass.	3/21/77	105
Amelia Eaton U.S. Customs Service 6 World Trade Center	3/22/77	205

New York, N.Y.		
Martin Youngberg 5 Richard Court Lincoln Park, N.J.	3/23/77	329
Kenneth Schaden 9318 Girdle Road Middlefield, Ohio	3/23/77	371

In addition to the foregoing witnesses, counsel for both sides stipulated on 3/23/77 at pages 324-5 of the transcript that Edward Feder, import specialist for the U.S. Customs Service, would testify as therein stated. Respondents, as anticipated, called no witnesses in their behalf.

During the hearing complaint counsel introduced approximately 121 exhibits and respondents approximately 18, all during the case-in-chief. When the case-in-chief was closed (Tr. 395), respondents' counsel stated that because respondent Banci had informed him that he had neither the time nor the finances to properly defend this matter, respondents would have nothing further to offer in evidence except a record of the 1970 testimony of Professor Rota in a similar proceeding before this Commission (Dkt. 8801). (Tr. 395-6). The latter was excluded from evidence but with permission for respondents to re-offer it by written motion with an explanatory brief, for reconsideration (Tr. 396). [xvii]

On 4/5/77 respondents filed their motion to admit into evidence Professor Antonio Rota's testimony on 7/29/70 at pp. 966-1036 of the transcript in D. 8801, arguing that Professor Rota's testimony would be relevant to the alleged willfulness of respondents' mislabeling here and that Rota, an Italian citizen, was "unavailable" within the meaning of Rule 804(a)(5) and 804(b)(1) of the new Federal Rules of Evidence. Complaint counsel's reply, filed 4/12/77 argued that Professor Rota was not "unavailable" merely because he resides in Italy and in any event his testimony would be of little value or positively misleading, chiefly because it was originally addressed to a different issue (unavoidable manufacturing variations despite due care) and, being seven years old, might be quite inaccurate at present. On 4/21/77 the administrative law judge denied respondents' motion to reconsider the admissibility of Professor Rota's former testimony, holding that Rota was not "unavailable" within the meaning of F.R.E. Rule 804(a)(5) and that the offer also seemed like a back-door effort to get into the field of unavoidable manufacturing defects, from exploring which respondents had been precluded by the order of 11/23/76 (for failure to make discovery on such subject). Finally the judge agreed that Rota's testimony, being quite out of date, could be misleading, absent opportunity for cross-examination thereof.

There followed a period of incomprehensible length while the reporting contractor attempted several times to correct a number of errors in the transcript, particularly the numerical pagination thereof. It was not until 8/18/77 that a stipulation of transcript corrections could be entered into and incorporated into the record by the administrative law judge. On 8/24/77 the record was officially closed. [xviii]

Pursuant to earlier arrangements (Tr. 398) complaint counsel on 9/20/77 filed their proposed findings of fact, conclusion of law, and order, with arguments in support thereof. An order issued on 10/12/77 noting respondents' default in serving proposed findings and conclusions but on the same date said proposals were actually filed, curing the default. At the same time respondents advised that on 9/2/77 respondent Banci's manufacturing vehicle, Lanificio Walter Banci s.a.s., had been adjudicated bankrupt. At the same time respondents filed their corresponding proposals. On 11/1/77 complaint counsel filed their proposed reply findings and brief.

Appendix

APPENDIX II
REPRESENTED vs. ACTUAL FIBER CONTENT
Selected Samples of Fabrics Imported into the United States by Respondents, 1973 and 1974
Group I

Item	Col. 1 Sample	Col. 2 Quality	Col. 3 Reference	Col. 4 Quantity (yards)	Col. 5 Year	Col. 6 Reference	Col. 7 Sample Source	Col. 8 Reference	Col. 9 Represented Content	Col. 10 Reference	Col. 11 Test Report	Col. 12 Reference	Col. 13 Deviation (in percentage points)
(1)	CX 5	Sloan (#[illegible])	RA I, 939	N/A a/	1973	N/A	Bobbie Brooks, Inc.	RA III, 93	50% Cotton 35% Polyester 15% Nylon	RA III, 931	33.9% Cotton 42.5% Polyester 23.6% Nylon	CX 1119	-16.1% Cotton + 7.5% Polyester + 8.6% Nylon
(2)	CX 9	Sloan (#27876)	RA I, 939	N/A	1973	N/A	Bobbie Brooks, Inc.	RA III, 97	50% Cotton 35% Polyester 15% Nylon	RA III, 931	43.8% Cotton 31.0% Polyester 25.2% Nylon	CX 1120	- 6.2% Cotton - 4.0% Polyester +10.2% Nylon
(3)	CX 10	Sloan (#29373)	RA I, 939	N/A	1973	N/A	Bobbie Brooks, Inc.	RA III, 98	50% Cotton 35% Polyester 15% Nylon	RA III, 931	40.7% Cotton 33.8% Polyester 25.5% Nylon	CX 1118	- 9.3% Cotton - 1.2% Polyester +10.5% Nylon
(4)	CX 11	Sloan (#31613)	RA I, 939	N/A	1973	N/A	Bobbie Brooks, Inc.	RA III, 99	50% Cotton 35% Polyester 15% Nylon	RA III, 931	40.5% Cotton 34.5% Polyester 25.0% Nylon	CX 1118	- 9.5% Cotton - .5% Polyester +10.0% Nylon
(5)	CX 12	Sloan (#31726)	RA I, 939	N/A	1973	N/A	Bobbie Brooks, Inc.	RA III, 910	50% Cotton 35% Polyester 15% Nylon	RA III, 931	41.0% Cotton 33.3% Polyester 25.7% Nylon	CX 1120	- 9.0% Cotton - 1.7% Polyester +10.7% Nylon
(6)	CX 13	Sloan (#31512)	RA I, 939	N/A	1973	N/A	Bobbie Brooks, Inc.	RA III, 911	50% Cotton 35% Polyester 15% Nylon	RA III, 931	36.1% Cotton 40.4% Polyester 23.5% Nylon	CX 1120	-13.9% Cotton + 5.4% Polyester + 8.5% Nylon
(7)	CX 47	Sloan	RA V, 916	9018 6/8	1973	RA I, 9623	U.S. Customs Entry #200050	RA V, 916	50% Cotton 35% Polyester 15% Nylon	RA III, 931	29.4% Cotton 44.4% Polyester 26.2% Nylon/Rayon	CX 129	-20.6% Cotton + 9.4% Polyester +11.2% Nylon
(8)	CX 48	Sloan	RA V, 917	6032 2/8	1973	RA I, 9624	U.S. Customs Entry #211358	RA V, 917	50% Cotton 35% Polyester 15% Nylon	RA III, 931	31.1% Cotton 41.7% Polyester 27.2% Nylon/Rayon	CX 130	-18.9% Cotton + 6.7% Polyester +12.2% Nylon
(9)	CX 49	Sloan	RA V, 918	26891 6/8	1973	RA I, 9610	U.S. Customs Entry #228514	RA V, 918	50% Cotton 35% Polyester 15% Nylon	RA III, 931	33.8% Cotton 36.6% Polyester 29.6% Nylon/Rayon	CX 131	-16.2% Cotton + 1.6% Polyester +14.6% Nylon
(10)	CX 50	Sloan	RA V, 919	[illegible]	1974	RA I, 9615	U.S. Customs Entry #255982	RA V, 919	50% Cotton 35% Polyester 15% Nylon	RA III, 931	32.7% Cotton 33.9% Polyester 33.4% Nylon/Rayon	CX 132	-17.3% Cotton - 1.1% Polyester +18.4% Nylon
(11)	CX 51	Sloan	RA V, 920	11368 6/8	1974	RA I, 9632	U.S. Customs Entry #281654	RA V, 920	50% Cotton 35% Polyester 15% Nylon	RA III, 931	31.3% Cotton 36.7% Polyester 32.0% Nylon/Rayon	CX 133	-18.7% Cotton + 1.7% Polyester +17.0% Nylon
(12)	CX 52	Sloan	RA V, 921	[illegible] 4/8	1974	RA I, 9616	U.S. Customs Entry #293029	RA V, 921	50% Cotton 35% Polyester 15% Nylon	RA III, 931	23.5% Cotton 47.6% Polyester 29.1% Nylon/Rayon	CX 134	-26.5% Cotton +12.6% Polyester +14.1% Nylon
(13)	CX 53	Sloan	RA V, 922	19753 2/8	1974	RA I, 9617	U.S. Customs Entry #297881	RA V, 922	50% Cotton 35% Polyester 15% Nylon	RA III, 931	10.6% Cotton 56.9% Polyester 32.7% Nylon/Rayon	CX 135	-39.4% Cotton +21.9% Polyester +17.7% Nylon
(14)	CX 54	Sloan	RA V, 923	20,090 6/8	1974	RA I, 9618	U.S. Customs Entry #282919	RA V, 923	50% Cotton 35% Polyester 15% Nylon	RA III, 931	26.4% Cotton 43.5% Polyester 30.1% Nylon	CX 136	-23.6% Cotton + 8.5% Polyester +15.1% Nylon
(15)	CX 56	Manito	RA V, 925	6,219	1974	RA I, 9636	U.S. Customs Entry #351718	RA V, 925	50% Cotton 35% Polyester 15% Nylon	RA III, 930	33.2% Cotton 45.2% Polyester 21.6% Nylon	CX 138	-16.8% Cotton +10.2% Polyester + 6.6% Nylon
(16)	CX 57	Manito	RA V, 926	25,118	1974	RA I, 9635	U.S. Customs Entry #390120	RA V, 926	50% Cotton 35% Polyester 15% Nylon	RA III, 930	29.3% Cotton 46.0% Polyester 21.6% Nylon	CX 139	-20.7% Cotton +11.0% Polyester + 6.6% Nylon
(17)	CX 83	Manito	RA V, 932	32,216 6/8	1974	RA I, 9621	U.S. Customs Entry #467125	RA V, 912	50% Cotton 35% Polyester 15% Nylon	RA III, 930	37.6% Cotton 25.0% Polyester 13.7% Nylon 26.7% Acrylic	CX 145	-17.6% Cotton -10.0% Polyester - 1.3% Nylon +26.7% Acrylic

a/ Figures not available

Item	Col. 1 Sample	Col. 2 Quality	Col. 3 Reference	Col. 4 Quantity (yards)	Col. 5 Year	Col. 6 Reference	Col. 7 Sample Source	Col. 8 Reference	Col. 9 Represented Content	Col. 10 Reference	Col. 11 Test Report	Col. 12 Reference	Col. 13 Deviation (in percentage points)
(18)	CX 55	Navajo	BA V, 926	28,770 2/8	1976	BA I, 9633	U.S. Customs Entry #329884	BA V, 926	40% Cotton 40% Polyester 20% Nylon	BA III, 938	16.4% Cotton 49.8% Polyester 33.8% Nylon	CX 137	-23.6% Cotton + 9.8% Polyester +13.8% Nylon
(19)	CX 58	Navajo	BA V, 927	26,093	1976	BA I, 9638	U.S. Customs Entry #360408	BA V, 927	40% Cotton 40% Polyester 20% Nylon	BA III, 938	19.1% Cotton 49.1% Polyester 31.8% Nylon	CX 140	-20.9% Cotton + 9.1% Polyester +11.8% Nylon
(20)	CX 59	Navajo	BA V, 928	24,676 6/8	1976	BA I, 9639	U.S. Customs Entry #364347	BA V, 928	40% Cotton 40% Polyester 20% Nylon	BA III, 938	22.1% Cotton 47.5% Polyester 30.4% Nylon	CX 141	-17.9% Cotton + 7.5% Polyester +10.4% Nylon
(21)	CX 60	Navajo	BA V, 929	49,388 2/8	1976	BA I, 9640	U.S. Customs Entry #365929	BA V, 929	40% Cotton 40% Polyester 20% Nylon	BA III, 938	24.9% Cotton 46.5% Polyester 28.6% Nylon	CX 142	-15.1% Cotton + 6.5% Polyester + 8.6% Nylon
(22)	CX 61	Navajo	BA V, 930	25,937 2/8	1976	BA I, 9619	U.S. Customs Entry #436157	BA V, 930	40% Cotton 40% Polyester 20% Nylon	BA III, 938	29.2% Cotton 39.9% Polyester 12.2% Nylon/Rayon 18.7% Acrylic	CX 143	-10.8% Cotton - .1% Polyester - 7.8% Nylon +18.7% Acrylic
(23)	CX 62	Navajo	BA V, 931	19,448 2/8	1974	BA I, 9630	U.S. Customs Entry #638319	BA V, 931	40% Cotton 40% Polyester 20% Nylon	BA III, 938	27.2% Cotton 44.3% Polyester 10.9% Nylon/Rayon 17.6% Acrylic	CX 144	-12.8% Cotton + 4.3% Polyester - 9.1% Nylon +17.6% Acrylic
(24)	CX 66	Verumba	BA V, 915	7618 4/8	1973	BA I, 9022	U.S. Customs Entry #180174	BA V, 915	65% Acrylic 25% Cotton 5% Nylon 5% Other Fibers	BA I, 9363	26.1% Acrylic 17.9% Cotton 48.6% Nylon/Rayon 7.6% Polyester	CX 128	-38.9% Acrylic - 7.1% Cotton +43.6% Nylon + 2.6% Polyester

Group 11

Line	Col. 1 Sample	Col. 2 Quality	Col. 3 Reference	Col. 4 Quantity (yards)	Col. 5 Year	Col. 6 Reference	Col. 7 Sample Source	Col. 8 Reference	Col. 9 Represented Content	Col. 10 Reference	Col. 11 Test Report	Col. 12 Reference	Col. 13 Deviation (in percentage points)
(25)	CE 19	Marcia (piece #93117)	RA III, 917	1913	1976	RA II, 9163	Melrose Mfg. Co.	RA II, 98 RA III, 917	55% Acrylic 20% Wool 20% Cotton 5% Other Fibers	RA III, 933	30.4% Wool 22.9% Cotton & Rayon 25.1% Acrylic 25.1% Nylon 13.1% Polyester	CE 112C	- 9.6% [illegible] + [illegible] Cotton [illegible] +[illegible] Other Fibers
(26)	CE 20	Marcia (piece #72876)	RA III, 918	N/A	1976	RA II, 9163	Melrose Mfg. Co.	RA II, 98 RA III, 918	55% Acrylic 20% Wool 20% Cotton 5% Other Fibers	RA III, 933	0.7% Wool 33.9% Cotton & Rayon 26.4% Acrylic 25.1% Nylon 19.4% Polyester	CE 112C	-1[illegible] Wool +11.9% [illegible] -28.6% Acrylic +37.5% Other Fibers
(27)	CE 21	Marcia (piece #[illegible])	RA III, 919	2080 6/8	1976	RA II, 925,104	Jones of Dallas Mfg.	RA II, 915 RA III, 919	55% Acrylic 20% Wool 20% Cotton 5% Other Fibers	RA III, 931	6.7% Wool 25.9% Cotton & Rayon 37.4% Acrylic 24.9% Nylon 7.1% Polyester	CE 112C	-13.3% Wool + 5.9% Cotton -1[illegible] Acrylic +27.0% Other Fibers
(28)	CE 22	Gretel (piece #64700)	RA III, 920	3930 2/8	1976	RA II, 926,165	Jones of Dallas Mfg.	RA II, 916 RA III, 920	55% Acrylic 20% Wool 20% Cotton 5% Other Fibers	RA III, 934	7.9% Wool 26.3% Cotton & Rayon 57.2% Acrylic 8.4% Nylon 6.2% Polyester	CE 112C	-12.1% Wool + 6.3% Cotton + 2.2% Acrylic + 5.6% Other Fibers
(29)	CE 23	Isabel (piece #497510)	RA III, 921	[illegible]	1976	RA II, [illegible], 166	Abbot Fabrics, Inc.	RA II, 947 RA III, 921	55% Acrylic 20% Wool 20% Cotton 5% Other Fibers	RA III, 933	6.4% Wool 26.7% Cotton & Rayon 34.6% Acrylic 23.2% Nylon 11.2% Polyester	CE 113C	-13.6% Wool + 6.7% Cotton -20.4% Acrylic [illegible] Other Fibers
(30)	CE 24	Marcia (piece #88127)	RA III, 922	1941	1976	RA II, 953, 167	Abbot Fabrics, Inc.	RA II, 948 RA III, 922	55% Acrylic 20% Wool 20% Cotton 5% Other Fibers	RA III, 933	0.7% Wool 25.2% Cotton & Rayon 30.3% Acrylic 26.7% Nylon 11.1% Polyester	CE 112C	-1[illegible] Wool + 5.2% Cotton -24.7% Acrylic +[illegible] Other Fibers
(31)	CE 25	Gretel (piece #49626)	RA III, 923	4657	1976	RA II, 954, 166	Abbot Fabrics, Inc.	RA II, 949 RA III, 923	55% Acrylic [illegible] Wool 20% Cotton 5% Other Fibers	RA III, 936	8.1% Wool 23.0% Cotton & Rayon 46.7% Acrylic 10.0% Nylon 11.6% Polyester	CE 113C	-11.9% Wool + 3.0% Cotton - 8.3% Acrylic +17.2% Other Fibers
(32)	CE 26	Isabel (piece #92260)	RA III, 924	[illegible] 7/8	1976	RA II, 987, 168	Arthro Sportswear, Inc.	RA II, 987 RA III, 924	55% Acrylic 20% Wool 20% Cotton 5% Other Fibers	RA III, 935	[illegible] Wool 28.0% Cotton & Rayon 22.9% Acrylic 24.8% Nylon 15.6% Polyester	CE 112C	-1[illegible] Wool + 8.0% Cotton -32.1% Acrylic +35.4% Other Fibers
(33)	CE 27	[illegible] (piece #[illegible])	RA III, 925	3372 6/8	1976	RA II, 988, 168	Arthro Sportswear, Inc.	RA II, 990 RA III, 925	55% Acrylic [illegible] Wool 20% Cotton [illegible]	RA III, 933	5.7% Wool 36.0% Cotton & Rayon 31.6% Acrylic 18.0% Nylon 11.4% Polyester	CE 112C	-14 [illegible] Wool +16.0% Cotton -23.4% Acrylic +23.4% Other Fibers
(34)	CE 28	[illegible] (piece #66702)	RA III, 926	[illegible]	1976	RA II, 9117, 169	P. Resnick, Inc.	RA II, 9117 RA III, 926	55% Acrylic [illegible] Wool 20% Cotton 5% Other Fibers	RA III, [illegible]	[illegible] Wool 28.2% Cotton & Rayon 28.1% Acrylic 32.0% Nylon 6.1% Polyester	CE 112C	-15.2% Wool + 8.2% Cotton -26.9% Acrylic +31.9% Other Fibers
(35)	CE 36	Isabel	RA V, 91	[illegible] 7/8	1976	RA I, 9600	U.S. Customs Entry #100540	RA V, 91	55% Acrylic 20% Wool 20% Cotton 5% Other Fibers	RA III, 933	[illegible] Wool 15.2% Cotton 33.5% Acrylic 37.3% Rayon/Nylon 6.4% Polyester	CE 113	-12.4% Wool - 4.8% Cotton -21.5% Acrylic +38.7% Other Fibers
(36)	CE 37	Bijou	RA V, 92	2332	1976	RA I, 9604	U.S. Customs Entry #103688	RA V, 92	55% Acrylic [illegible] Wool 20% Cotton 5% Other Fibers	RA III, 937	4.4% Wool 22.0% Cotton 47.9% Acrylic 11.6% Rayon/Nylon 14.3% Polyester	CE 118	-15.6% Wool + 2.0% Cotton - [illegible] Acrylic +20.[illegible] Other Fibers
(37)	CE 39	Isabel	RA V, 94	1600 6/8	1976	RA I, 9602	U.S. Customs Entry #106791	RA V, 94	55% Acrylic [illegible] Wool 20% Cotton 5% Other Fibers	RA III, 933	9.1% Wool 10.3% Cotton 36.2% Acrylic 17.0% Nylon/Rayon 7.2% Polyester	CE 117	-10 [illegible] Wool - 9.7% Cotton -18.8% Acrylic +19.2% Other Fibers
(38)	CE 38	Marcia	RA V, 95	[illegible] 2/8	1976	RA I, 9637	U.S. Customs Entry #[illegible]677	RA V, 95	55% Acrylic [illegible] Wool 20% Cotton 5% Other Fibers	RA III, 939	8.4% Wool 11.9% Cotton 55.9% Acrylic 15.7% Rayon/Nylon 8.1% Polyester	CE 110	-11.6% Wool - 8.1% Cotton + .9% Acrylic +18.8% Other Fibers

Item	Col. 1 Sample	Col. 2 Quality	Col. 3 Reference	Col. 4 Quantity (yards)	Col. 5 Year	Col. 6 Reference	Col. 7 Sample Source	Col. 8 Reference	Col. 9 Represented Content	Col. 10 Reference	Col. 11 Test Report	Col. 12 Reference	Col. 13 Deviation (in percentage points)
(39)	CX 37	Isabel	RA V, 96	1731 4/8	1974	RA I, 9603	U.S. Customs Entry #628331	RA V, 96	55% Acrylic 20% Wool 20% Cotton 5% Other Fibers	RA III, 933	2.9% Wool 10.1% Cotton 41.1% Acrylic 37.7% Rayon/Nylon 6.2% Polyester	CX 119	-17.1% Wool - 9.9% Cotton -13.9% Acrylic +38.9% Other Fibers
(40)	CX 38	Marnie	RA V, 97	3652 4/8	1974	RA I, 9604	U.S. Customs Entry #636156	RA V, 97	55% Acrylic 20% Wool 20% Cotton 5% Other Fibers	RA III, 933	9.0% Wool 21.3% Cotton 35.9% Acrylic 29.0% Nylon/Rayon 4.8% Polyester	CX 120	-11.0% Wool + 1.3% Cotton -19.1% Acrylic +28.8% Other Fibers
(41)	CX 39	Marnie	RA V, 98	5150 2/8	1974	RA I, 9605	U.S. Customs Entry #647209	RA V, 98	55% Acrylic 20% Wool 20% Cotton 5% Other Fibers	RA III, 933	.6% Wool 21.1% Cotton 45.7% Acrylic 25.8% Nylon/Rayon 6.8% Polyester	CX 121	-19.4% Wool + 1.1% Cotton - 9.3% Acrylic +27.6% Other Fibers
(42)	CX 40	Marnie	RA V, 99	2602 6/8	1974	RA I, 9608	U.S. Customs Entry #647216	RA V, 99	55% Acrylic 20% Wool 20% Cotton 5% Other Fibers	RA III, 933	9.5% Wool 14.0% Cotton 39.2% Acrylic 33.2% Nylon/Rayon 4.1% Polyester	CX 122	-10.5% Wool - 6.0% Cotton -15.8% Acrylic +32.3% Other Fibers
(43)	CX 41	Marnie	RA V, 910	1913	1974	RA I, 9609	U.S. Customs Entry #642599	RA V, 910	55% Acrylic 20% Wool 20% Cotton 5% Other Fibers	RA III, 933	11.0% Wool 17.4% Cotton 21.7% Acrylic 38.8% Rayon/Nylon 11.1% Polyester	CX 123	- 9.0% Wool - 2.6% Cotton -33.3% Acrylic +44.9% Other Fibers
(44)	CX 42	Marnie	RA V, 911	3372 6/8	1974	RA I, 9610	U.S. Customs Entry #662876	RA V, 911	55% Acrylic 20% Wool 20% Cotton 5% Other Fibers	RA III, 933	9.9% Wool 17.8% Cotton 34.3% Acrylic 28.8% Rayon/Nylon 9.2% Polyester	CX 124	-10.1% Wool - 2.2% Cotton -20.7% Acrylic +33.0% Other Fibers
(45)	CX 6	Eve	RA I, 919 RA III, 92	N/A	1973	RA III, 92	Fabri-Centers of America	RA III, 92	45% Acrylic 25% Wool 25% Cotton 5% Other Fibers	RA III, 929	7.3% Wool 19.0% Cotton 58.1% Acrylic 7.0% Nylon 5.3% Rayon 3.3% Polyester	CX 194	-17.7% Wool - 6.0% Cotton +13.1% Acrylic +10.6% Other Fibers
(46)	CX 33	Eve	RA V, 93	962 2/8	1973	RA I, 9614	U.S. Customs Entry #107155	RA V, 93	45% Acrylic 25% Wool 25% Cotton 5% Other Fibers	RA III, 929	10.8% Wool 19.7% Cotton 56.1% Acrylic 10.2% Nylon/Rayon 3.2% Polyester	CX 115	-14.2% Wool - 5.3% Cotton +11.1% Acrylic + 8.4% Other Fibers
(47)	CX 43	Eve	RA V, 912	3892 4/8	1974	RA I, 9611	U.S. Customs Entry #662870	RA V, 912	45% Acrylic 25% Wool 25% Cotton 5% Other Fibers	RA III, 929	7.2% Wool 5.9% Cotton 35.0% Acrylic 32.6% Rayon/Nylon 19.3% Polyester	CX 125	-17.8% Wool -19.1% Cotton -10.0% Acrylic +46.9% Other Fibers
(48)	CX 44	Eve	RA V, 913	6325 6/8	1973	RA I, 9612	U.S. Customs Entry #677950	RA V, 913	45% Acrylic 25% Wool 25% Cotton 5% Other Fibers	RA III, 929	12.3% Wool 17.1% Cotton 53.3% Acrylic 14.0% Rayon/Nylon 3.3% Polyester	CX 126	-12.7% Wool - 7.9% Cotton + 8.3% Acrylic +12.3% Other Fibers
(49)	CX 45	Eve	RA V, 914	2080 2/8	1973	RA I, 9613	U.S. Customs Entry #506770	RA V, 914	45% Acrylic 25% Wool 25% Cotton 5% Other Fibers	RA III, 929	12.5% Wool 16.4% Cotton 52.4% Acrylic 15.3% Rayon 3.4% Polyester	CX 127	-12.5% Wool - 8.6% Cotton + 7.4% Acrylic +13.7% Other Fibers

Group III

Item	Col. 1 Sample	Col. 2 Quality	Col. 3 Reference	Col. 4 Quantity (yards)	Col. 5 Year	Col. 6 Reference	Col. 7 Sample Source	Col. 8 Reference	Col. 9 Represented Content	Col. 10 Reference	Col. 11 Test Report	Col. 12 Reference	Col. 13 Deviation (in percentage points)
(50)	CX 64	Verusha	RA V, 933	2820 6/8	1973	RA I, 9625	U.S. Customs Entry #201672	RA V, 933	65% Acrylic 25% Cotton 5% Nylon 5% Other Fibers	RA I, 9382, 383, 385, 388, 392	29.2% Acrylic 17.4% Cotton 39.1% Nylon/Rayon 6.7% Polyester 7.6% Wool	CX 146	-35.8% Acrylic - 7.6% Cotton +34.1% Nylon + 9.3% Other Fibers
(51)	CX 65	Verusha	RA V, 934	7056	1973	RA I, 9626	U.S. Customs Entry #207164	RA V, 934	65% Acrylic 25% Cotton 5% Nylon 5% Other Fibers	RA I, 9395, 396, 398, 401, 403	24.6% Acrylic 22.4% Cotton 51.5% Rayon/Nylon 1.5% Wool	CX 147	-40.4% Acrylic - 2.6% Cotton +46.5% Nylon - 3.5% Other Fibers
(52)	CX 66	Verusha	RA V, 935	2902 2/8	1973	RA I, 9628	U.S. Customs Entry #218868	RA V, 935	65% Acrylic 25% Cotton 5% Nylon 5% Other Fibers	RA I, 9421, 422, 426, 427, 429	35.4% Acrylic 14.1% Cotton 36.7% Rayon/Nylon 6.2% Polyester 8.1% Wool	CX 148	-29.6% Acrylic -10.9% Cotton +31.7% Nylon + 9.3% Other Fibers
(53)	CX 67	Verusha	RA V, 936	6160	1973	RA I, 9629	U.S. Customs Entry #216060	RA V, 936	65% Acrylic 25% Cotton 5% Nylon 5% Other Fibers	RA I, 9430, 435, 437, 440, 442	35.7% Acrylic 14.6% Cotton 40.6% Rayon/Nylon 7.4% Polyester 1.9% Wool	CX 149	-29.3% Acrylic -10.4% Cotton +35.6% Nylon + 4.3% Other Fibers
(54)	CX 30	Verusha	RA III, 928	638	1973	RA III, 9170	Ivy Int'l Ltd	RA II, 9150	65% Acrylic 25% Cotton 10% Nylon	RA III, 9151	47.2% Acrylic 24.4% Cotton 21.1% Rayon/Nylon 3.4% Polyester 3.7% Acetate Wool	CX 1170	-17.8% Acrylic - .6% Cotton +11.1% Nylon + 3.4% Polyester + 3.7% Acetate Wool
(55)	CX 68	Ingrid	RA V, 937	8412 6/8	1973	RA I, 9631	U.S. Customs Entry #229792	RA V, 937	65% Acrylic 25% Cotton 5% Nylon 5% Other Fibers	RA III, 940	42.1% Acrylic 21.4% Cotton 27.5% Rayon/Nylon 6.0% Polyester 2.0% Wool	CX 150	-22.9% Acrylic - 3.6% Cotton +22.5% Nylon + 3.0% Other Fibers
(56)	[illegible]	Navajo	RA V, 938	24496 2/8	1974	RA I, 9607	U.S. Customs Entry #382323	RA V, 938	40% Cotton 40% Polyester 20% Nylon	RA III, 938	22.4% Cotton 36.7% Polyester 27.0% Rayon/Nylon 14.3% Acrylic 1.6% Wool	CX 151	-17.6% Cotton - 3.3% Polyester + 7.0% Nylon +15.9% Other Fibers
(57)	[illegible]	Navajo	RA V, 939	25,086 2/8	1974	RA I, 9636	U.S. Customs Entry #600430	RA V, 939	[illegible] 40% Polyester 20% Nylon	RA III, 939	24.9% Cotton 41.5% Polyester 11.9% Rayon/Nylon 20.6% Acrylic 1.1% Wool	CX 152	-15.1% Cotton + 1.5% Polyester - 8.1% Nylon +21.7% Other Fibers
(58)	CX 71	Nyla	RA V, 941	14,891 2/8	1974	RA I, 9606	U.S. Customs Entry #667214	RA V, 941	70% Acrylic 25% Cotton 5% Other Fibers	RA III, 941	57.0% Acrylic 17.6% COtton 19.9% Rayon/Nylon 3.6% Polyester 1.9% Wool	CX 153	-13.0% Acrylic - 7.4% Cotton +20.4% Other Fibers

OPINION OF THE COMMISSION

BY DIXON, *Commissioner*:

This case principally involves the question of whether the Commission can and should apply provisions of the Wool Products Labeling Act of 1939 (15 U.S.C. 68) and the [2] Textile Fiber Products Identification Act (15 U.S.C. 70) which empower the Commission to require an importer that has violated those acts to post a bond with the Treasury Department in double the amount of future imports as a guarantee against further violations of the law.

The complaint in this matter was issued June 24, 1975, and charged respondents with a variety of violations of the Wool and Textile Acts, as well as Section Five of the Federal Trade Commission Act (15 U.S.C. 45) in connection with the importation from Italy into the United States of various wool and other textile fiber products. Protracted pretrial skirmishing followed by a short and peaceful trial before Administrative Law Judge (ALJ) Paul Teetor led to his initial decision sustaining in large measure the allegations of the complaint. Judge Teetor found that respondents had violated the Wool Act, after review of numerous samples of wool products which evidence substantial overstatements of their wool content. He found that respondents had violated the Textile Act upon consideration of numerous fabric samples evidencing substantial overstatements of the content of textile fibers other than wool. Based upon these violations, the ALJ recommended entry of an order requiring that respondents cease and desist from future violations and, in addition, post a bond in double the value of future imports to be forfeited in the event of further violations of the Wool and Textile Acts.

Judge Teetor also found that respondents had violated Section Five by misrepresenting the shrinkage factor of certain of their imports and recommended that an order enter prohibiting that practice.

The ALJ rejected complaint allegations that misstatements of the amount of non-wool fibers in wool products constituted violations of Section 5 of the Federal Trade Commission Act, and that misstatements of wool content on sales invoices of wool products constituted Section 5 offenses. Judge Teetor also rejected the argument that *understatements* of textile fiber components violated the Textile Act. Complaint counsel have appealed each of these adverse rulings, while respondents have objected to imposition of the bond and the finding of Section 5 liability for misrepresentation of shrinkage factor. Our disposition of these appeals follows: [3]

Bond Requirement

The record reveals that 58 samples were taken from shipments totalling over 1,185,000 yards of woolen and other textile products. (I.D. 17)[1] Of these 58 samples, 25 were represented to and did include some wool. (I.D. 27) In 23 of the wool samples, wool content was overstated by 10 to 20 percentage points.[2] In the other two the overstatement was 3-10%. (I.D. 31)[3] Another group of 24 textile samples, as to which no wool content was either claimed or found by testing, involved 29 overstatements of fiber content in excess of 3%, including 8 overstatements of fiber content in excess of 20%. (I.D. 28)[4] The ALJ found that [4] these substantial and pervasive overstatements of wool and textile fiber content constituted violations of the Wool and Textile Acts respectively. (I.D. pp. 29, 31-32)

Section 8 of the Wool Products Labeling Act, 15 U.S.C. 68f, provides in relevant part that, with respect to fiber content information which the Act requires to be disclosed:

> any person who falsifies, or fails to set forth, said information in said invoices, or who falsifies or perjures said consignee's declaration insofar as it relates to said information, may thenceforth be prohibited by the Commission from importing, or participating in the importation of, any wool products into the United States except upon filing bond with the Secretary of the Treasury in a sum double the value of said wool products and any duty thereon, conditioned upon compliance with the provisions of this Act.

Section 9 of the Textile Fiber Products Identification Act, 15 U.S.C. 70g, provides in relevant part that, with respect to information required to be provided by a seller of textile products:

> any person who falsifies, or perjures the consignee's declaration insofar as it relates to such information, may thenceforth be prohibited by the Commission from importing, or participating in the importation of, any textile fiber product into the United States except upon filing bond with the Secretary of the Treasury in a sum double the value

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[1] The following abbreviations are used herein:

I.D.	– Initial Decision Finding of Fact No.
I.D. p.	– Initial Decision Page No.
Tr.	– Transcript of Testimony, Page No.
CX	– Complaint Counsel's Exhibit No.
RX	– Respondent's Exhibit No.

[2] – referring to an overstatement or understatement of fiber content by "x" percent, we mean that the number representing the indicated percentage of wool exceeds or falls short of the actual percentage of wool in the product by the number "x". Thus, a claim that a product with 20% wool contains 40% wool is considered an overstatement of "20%", although one might also view it as overstating the wool content by 100%.

[3] Those samples involving misstatements of wool content also involved 41 misstatements of non-wool fibers, including 29 overstatements, of which 10 were in excess of 20 percentage points. (I.D. 32-33) Judge Teetor found no violation based on these misstatements. We discuss them in regard to complaint counsel's appeal, infra at p. 13.

[4] As a corollary, these samples also contained numerous understatements of textile fiber content in excess of 3% (I.D. 29). Judge Teetor concluded that these understatements did not violate the law. Our discussion of this point occurs infra at p. 15.

of said products and any duty thereon, conditioned upon compliance with the provisions of this Act.

The purpose of these provisions is to allow the Wool and Textile Acts to be enforced against previous violators who may be, by virtue of their status as importers with assets outside and unreachable from the United States, immune, in practice, to the threat of civil penalties (the ordinary mode of enforcement of orders to cease and desist. [5]

The applicability of the bonding provisions to the facts of the instant case is clear. Respondent Banci is an Italian citizen, while the corporate respondents appear dormant within the United States. It thus seems quite likely that the threat of civil penalties would do little to deter a resumption of misbranding in the future by the individual or corporations through which he might act. Need for the bond is further enhanced by the fact that respondents have evidenced a pattern of repeated violations of the labeling laws (despite notifications from U.S. Customs) at least since 1972, notwithstanding their promise in 1971 (in conjunction with dismissal of previous misbranding charges) that they would undertake to comply with the labeling laws. *Verrazzano Trading Corp., et al.*, 78 F.T.C. 637, 675 (1971). As Judge Teetor properly observed, imposition of a bond, to be forfeited in the event of further violations, appears to be the only way to ensure respondents' compliance with the Wool and Textile Acts. (I.D. p. 48)

Respondents argue that imposition of a bond requires a finding that the law has been willfully breached. This is belied by the plain language of the statutes, which applies to a party who "*falsifies or* perjures" the consignee's declaration.[5] While perjury, of course, denotes an element of willfullness, falsification may occur by design or otherwise.[6] To read into the term a necessary element of intent would render its use in the statute redundant.[7] The plain meaning of the statute is, moreover, wholly consistent with its plain purpose. It is apparent that misbranding that results from recklessness, [6] carelessness, or incompetence is no less inimical to the public interest than that which is done with specific intent to deceive. The careless violator is no less dangerous, and no less likely to repeat its unlawful carelessness or heedlessness, than the willful one.[8] Accordingly, it comports fully with the statutory scheme that the bonding requirement should apply to misbranding whether intentional or not.

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[5] In addition, the Wool Act authorizes imposition of a bond where the importer has falsified or failed to set forth the requisite information in its customs invoices.

[6] Webster's *New International Dictionary* (2d ed.) defines "falsify" as "To make false; specif. (a) to represent falsely . . ." at page 915.

[7] It would also lead to different constructions of "falsify" in different Sections of the Acts. For example, Section 4(c) of the Textile Act (15 U.S.C. 70b) defines a textile product to be "falsely or deceptively" advertised if, without regard to the advertiser's intent, information required by the statute is omitted from the advertisement.

Respondents also observe that the bonding provision of the Wool Act may be invoked for falsification only of the *consignee's declaration* or the special invoices required by the Tariff Act of 1930, while the Textile Act bonding provision is triggered by falsification only of the consignee's declaration. Respondents contend that the ALJ did not find that these particular customs documents had been falsified.

While the ALJ did not focus precisely on this technical point, the requisite finding of falsification is implicit in the initial decision, and, in any event, our own review of the record leaves no doubt that the relevant invoices and consignee's declarations were falsified. The ALJ found, in "Appendix II" of his initial decision and the findings which summarize it, that misbranding of numerous fabrics had occurred. Respondents admitted before trial (RA III, ¶ 29-41; 9/20/76) and did not dispute at trial, that the representations found by the ALJ to be false had been made on "all fiber content tags, supplier's invoices, special customs invoices and consumption entries . . ." relating to each fabric in question. From this it is clear that falsification of supplier's and special customs invoices occurred, as required for imposition of a bond under the Wool Act. It is also clear that falsification of consignee's declarations occurred. The consignee's declaration is merely a sworn statement contained in the consumption entry in which the importer vouches for the accuracy of the invoices accompanying the entry (*e.g.*, CX 73E). Falsification of the invoices is tantamount to falsification of [7] the consignee's declaration. Accordingly, we find that falsification of supplier's invoices, special customs invoices, and consignee's declaration has occurred with respect to all fabrics found by the ALJ to have been misbranded.

Constitutionality of Bond Requirement

Respondents also contend that the bonding provisions of the Wool and Textile Acts are unconstitutional. The ALJ refused to address the merits of this argument, concluding that it would be inappropriate for an administrative agency to consider the constitutionality of one of its organic statutes. Wishing to preserve our options pending further consideration of this issue, the Commission instructed both sides to brief the merits of the constitutional argument, subject to the Commission's determination as to whether it should be considered.

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[8] That Congress clearly recognized the distinction between the two kinds of behavior is evident from Section 10 of the Wool Act (15 U.S.C. 68h) and Section 11 of the Textile Act (15 U.S.C. 70h) which impose criminal penalties for "Any person who willfully" violates various provisions of the laws, including Section 8 of the Wool Act and Section 9 of the Textile Act.

With all the arguments now in hand, we find it much easier to answer the constitutional question than to decide whether we ought to ask it. While the Commission is frequently called upon to assess the impact of constitutional provisions upon various proposed *interpretations* of its organic statutes, or *orders* proposed to remedy violations of those statutes [*e.g., National Commission on Egg Nutrition,* 88 F.T.C. 84 (1976); *aff'd and ordered enforced as modified,* 570 F.2d 157 (7th Cir. 1977)] the situation presented here is somewhat different, because respondents squarely challenge the constitutionality of an entire provision of law, however applied, and adoption of their position would lead to non-enforcement under any circumstances of a provision which Congress and the President believed to pass constitutional muster.

As complaint counsel and the administrative law judge contend, there is considerable case law support for the view that an administrative agency lacks jurisdiction or authority to consider the constitutional validity of the statutes it enforces, *e.g., Johnson* v. *Robison,* 415 U.S. 361, 368 (1974); *Public Utilities Commission* v. *United States,* 355 U.S. 534, 539 (1958); *Macy Industries, Inc.,* 51 F.T.C. 931, 151 (1955), *aff'd,* 355 U.S. 411 (1958). Policy reasons justifying such an approach are readily imagined. However, viewed, an [8] administrative agency is created to enforce the law and effect the mandate of Congress. Were an agency to conclude that a duly enacted statute was unconstitutional, it might thereby preclude any review of that issue by the courts, thus thwarting a constitutional scheme which contemplates passage of laws by Congress, enforcement of them by the executive, and ultimate determination of their constitutionality by the judiciary.

There are, however, persuasive reasons which argue in favor of constitutional consideration by administrative agencies. For one thing, Commissioners, like other federal officials, take an oath of office to "support and defend the Constitution," which presumably entails that we not wholly ignore its effect, when relevant, upon contemplated action. It may be argued that in upholding the Constitution, the administrative agency should defer in the first instance to the judgment of Congress as to what the Constitution means. This approach contains much to recommend it in the absence of relevant case law. However, one may imagine many situations, short of an adverse Supreme Court ruling directly on point, in which the unconstitutionality of a statute would be strongly indicated to all reasonable minds. For example, one might ask what would happen if, (to take a pure hypothetical) during the pendency of this litigation the Supreme Court were to rule unconstitutional the bonding provisions of the Fur Products Labeling Act, 15 U.S.C. 69, 69d, a statute closely analogous in form and purpose to the Wool and Textile Acts. Such a ruling might well compel any reasonable person to conclude that the bond provisions of the Wool and Textile Acts must fall. It is only a matter of degree to move from precedents of this sort to the less pointed precedents which defense counsel may believe warrant condemnation of the statute here or others that might be challenged. It is no secret that certain statutes fall into disuse because prosecutors conclude, from their reading of case law and in the exercise of largely unreviewable discretion, that the constitutionality of those statutes could not survive challenge. It seems an artificial distinction to maintain that an administrative agency cannot consider the same issues when it acts, on the record for all to see, in its adjudicative capacity. [9]

Moreover, as pointed out in the article upon which respondents rely for support,[9] there may be instances in which agency review of constitutional issues will furnish the informed factual and legal basis that is needed for reviewing courts to reach the best decision when they must face the constitutional question. Perhaps the lesson to be drawn from these conflicting observations is that administrative agencies ought not blind themselves to constitutional considerations, but in taking them into account they should give extreme deference to the implicit view of Congress that such statutes are constitutional, so as to avoid thwarting the Congressional intent by precluding judicial review of a statute's constitutionality.

Fortunately for the Commission, this is not a case in which we need risk bringing the pillars of the republic crashing down about our ears. Having considered respondents' sketchy constitutional arguments, we find them without merit, and we can thus discern no reason to question the determination of Congress that the bond provisions of the Wool and Textile Acts are constitutionally sound.

Respondents appear to contend that the bonding provisions constitute a denial of due process because they restrain unreasonably, or without need, respondents' ability, if not "right" to engage in the importation of fabrics. Implicit in this part of the argument is also an equal protection claim, that importers have been impermissibly singled out for imposition of the bond requirement. As complaint counsel observe, however, there is no vested right to carry on foreign commerce with the United States and the power of Congress over foreign commerce is plenary. *United States* v. *12 200-Ft. Reels of Film,* 413 U.S. 123, 125–6 (1973). Given that Congress might, if it chose, exclude all foreign imports, *Buttfield* v. *Stranahan,* 192 U.S. 470, 493 (1904), it can surely place less restrictive conditions upon importers found to have violated federal labeling laws without offending due process.[10]

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[9] *Note*, "The Authority of Administrative Agencies to Consider the Constitutionality of Statutes," 90 Harv. L. Rev. 1682 (1977).

[10] Nor do the bond provisions discriminate impermissibly. While the necessity to post a bond imposes some incremental restraint upon an importer's ability or inclination to import, the requirement is clearly tailored reasonably to ensure non-repetition of previous violations by a class of violators which may reasonably be thought less likely than others to be amenable to the sanctions ordinarily imposed for violations of an order. *Metropolitan Casualty Insurance Co.* v. *Brownell,* 294 U.S. 580, 584 (1935). Although respondents claim that Italian law would permit enforcement of a civil penalty judgment against them rendered by an American court, the ease with which this might be accomplished is by no means clear, and surely the process would be fraught with much greater uncertainty and expense than that by which civil penalties are ordinarily exacted. Under the circumstances, we think that Congress quite reasonably provided an alternative means to ensure deterrence of repeat violations by importers, and its judgment in this matter affecting foreign commerce is one that ought not lightly be disturbed, cf. *Mathews* v. *Diaz,* 426 U.S. 67, 78–82 (1976).

Finally, we reject respondents' contention that the relevant provisions of law are impermissibly vague. Counsel's strained attempts to misunderstand what these provisions mean are perhaps the best indication of their clarity.

For the foregoing reasons we are unpersuaded by respondents' constitutional challenge, assuming *arguendo* that we ought to consider it. [11]

Misrepresentation of Shrinkage Factor

The administrative law judge found that respondents had violated Section 5 by misrepresenting the residual shrinkage of large quantities of cloth sold to Bobbie Brooks and other purchasers. (I.D. 8, 36) The fabric in question was represented as possessing residual shrinkage of 1% to 1-1/2%, when, in fact, it was likely to shrink by 5-6%. (I.D. 36)

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[10] This consideration also speaks to respondents' argument that the bond constitutes an unconstitutionally severe "penalty."

There is no serious dispute as to the existence of the misrepresentation, or its materiality. Fabric with a residual shrinkage of less than 1-1/2% is suitable for immediate incorporation in clothing, and implies to the manufacturer some sort of pre-treatment, for which additional payment may be warranted. Fabric with residual shrinkage approaching 6% is not suitable for incorporation in many kinds of clothing without further treatment, since washing may result in substantial shrinkage that would materially alter the size of the clothing. (I.D. 37)

While not challenging these facts, respondents appear to contend that what is involved is merely a "private controversy" which injured no consumers. Respondents contend that Bobbie Brooks tested the cloth itself before making any use of it, so that it was aware of its true shrinkage factor. Any transmission of the fabric untreated to the public was, therefore, the responsibility of the manufacturer.

The principal point to be made about all this, we think, is that Section 5 does not tolerate deceptive practices by businesses merely because they are visited upon other businesses rather than directly upon consumers. In either case the public is harmed. The law prohibits deceptive practices affecting commerce because such practices make it impossible for purchasers to make the informed buying decisions that are needed to maximize the welfare of all citizens in a capitalist economy. These market-distorting effects of deception are no less significant in the middle of the chain of distribution than they are at its end. If a manufacturer pays extra money for fabric because it is represented to be pre-shrunken, that cost must inevitably be [12] passed along to the consuming public, in one form or another. Deceptive practices which alter the buying patterns of manufacturers must inevitably affect, in turn, the way such manufacturers relate to their customers.[11]

It is true, of course, that manufacturers may be in a better position than consumers to pursue private remedies to redress the effects of deception. For this reason, the Commission, in the exercise of its discretion, may be less inclined to pursue deceptions occurring between businesses. However, this can in no way constitute a legal defense to charges of misrepresentation. The deception challenged here occurred with respect to a substantial volume of commerce (I.D. 36), and in addition to Bobbie Brooks involved at least one other customer of respondents, and may well have involved numerous customers to whom respondents made representations of shrinkage. (I.D. p. 37) It is obviously in the public interest that such practices be curbed. [13]

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[11] This is true even where the deception is detected by the manufacturer and not passed on to consumers. With respect to the shrinkage problem, we think that while Bobbie Brooks may be sufficiently large to test its own fabrics for shrinkage, other, smaller manufacturers might well not be in a position to detect such misrepresentations, and might, therefore, pass them on directly to consumers. This, then, is a further potential source of injury from respondents' practice.

Complaint Counsel's Appeal – Section Five Labeling Violations

Nine samples of respondents' fabrics were tested and found to contain small, undisclosed traces of wool ranging from 1.1% to 9.6% (I.D. 34). These samples also exhibited 16 substantial overstatements of the percentage of non-wool fabrics, including 5 overstatements in excess of 20 percentage points. (I.D. 35). In addition, as noted *supra* at n. 3, those fabric samples in which wool content was overstated also involved 29 overstatements of fiber content other than wool. The complaint alleged that the overstatements of non-wool fibers constituted violations of Section 5 of the Federal Trade Commission Act.[12]

The administrative law judge dismissed the Section 5 count on grounds that a deceptive tendency required under Section 5 could not be inferred from "mere misbranding alone." We reverse.

Misstatements of the fiber content of fabrics are, by definition, "misrepresentations," and that misrepresentations of more than *de minimis* character may be materially misleading is, we think, equally clear. The fiber composition of a fabric is likely to affect its perceived value in the eyes of both some manufacturers and some consumers. Perhaps the best indication of this comes from the customs invoices present in the record of this case. In these, respondents [14] declared both the fiber percentage composition by *weight* of their products, and the fiber percentage composition by *value*. As might be supposed, different fabrics have different relative values. Thus, for example, respondents' Navajo was represented to consist of 40% cotton, 40% polyester, and 20% nylon. However, 86% of the *value* of the same fabric was declared to be accounted for by cotton (9% by polyester, and 5% by nylon) because of the greater relative value of cotton. (CX id 102I). In fact, none of the samples of Navajo present in the record contain anything approaching 40% cotton. Some contain less than 25% cotton, one only 22.4% cotton (CX 69), which means that the *value* of this fabric was implicitly overstated to a very substantial degree. Misrepresentations of fiber content may thus lead manufacturers and consumers to misestimate the value of the fabrics they are purchasing, as well as their characteristics. We believe, accordingly, that such misrepresentations possess the capacity to mislead consumers materially.

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[12] These violations were alleged under Section 5 upon the theory that the decision in *Marcus* v. *Federal Trade Commission*, 354 F.2d 85 (2d Cir. 1965) precluded a finding of Wool Act violation for mislabeling of the non-wool content of wool products, while the Textile Act does not apply to products which contain wool. Recognizing the enforcement vacuum created by its holding, the Court of Appeals invited the Commission to fill it by use of Section 5's proscription of deceptive acts or practices. (354 F.2d 85 at p. 88 n. 4)

While the materiality of a misrepresentation is clearly a matter which the Commission, in its expertise, may infer, *Federal Trade Commission* v. *Colgate-Palmolive Co.,* 380 U.S. 374, 392 (1965); *Leonard F. Porter, Inc., et al.,* 88 F.T.C. 548, 628 (1976), we need not rely in this instance solely upon such inference to support our conclusion. The same conclusion has been reached by Congress when it passed the Wool and Textile Acts. These laws are premised upon a clear determination that accurate fiber content information is an important factor in consumer purchase decisions. See, *e.g.,* Report to Accompany H.R. 944, Committee on Interstate and Foreign Commerce, 76th Cong., 1st Sess., Report 907, 1939; Report of Senate Committee on Interstate and Foreign Commerce, 85th Cong., 2d Sess., Report 1658, June 6, 1958; Report to Accompany H.R. 469, Committee on Interstate and Foreign Commerce, 85th Cong., 1st Sess., August 5, 1957. Accordingly, by holding that misrepresentations of non-wool fiber content constitute violations of Section 5, the Commission does no more than give effect to the Congressional determination that these practices are misleading and may tend to injure consumers.[13] [15]

While the foregoing findings are adequate to address complaint counsel's appeal,[14] we must note that having again considered the Second Circuit's holding in the *Marcus* case, we respectfully question whether it is an appropriate interpretation of the law. [16]

The Second Circuit in *Marcus* held that the Wool Act was concerned only with protecting buyers against substitution of inferior products for wool. Where the wool content was not overstated, the court held that no violation could result merely because of misstatement of the content of other, "inferior" fibers. In reaching this conclusion, the Court sought to overcome Section 4(a)(2)(A)(4) of the Wool Act which defines a wool product to be misbranded if it lacks a stamp, tag, or label which shows, *inter alia*,

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[13] We also hold that misrepresentations of both wool and non-wool fibers in sales invoices constitute violations of Section 5. While the Wool Act does not extend to sales invoices, the misrepresentations contained therein may be no less misleading to consumers than those made on the label or in customs documents covered by the Act. See *G. Sherman Corp., et al.,* 56 F.T.C. 783, 786 (1960); cf. *Grand Union Co.* v. *FTC,* 300 F.2d 92, 98 (2d Cir. 1962).

[14] Complaint counsel have also argued on appeal that understatements of textile fibers should also be considered violations of the Textile Act. The ALJ concluded they were not violations, analogizing from *Marcus* v. *Federal Trade Commission, supra* which held that understatements of *wool* content were not violations of the Wool Act. The Second Circuit's rationale was that the Wool Act was designed only to protect consumers who viewed wool as a desirable component product and who would presumably not be injured if wool content were understated. This holding is patently not generalizable to the Textile Act, which is designed to ensure accurate disclosure of the constituent fibers in textile products and embodies no assumption as to which fibers consumers will prefer. Obviously understatements of *disfavored* fibers may be just as deceptive and injurious as overstatements of *preferred* fibers. Accordingly, we believe that understatements of fiber content constitute violations of the Textile Fiber Products Identification Act. However, the point may be of little significance for most proceedings. The existence of an understatement of one fiber is likely to ensure the existence of an overstatement of at least one other, since even a manufacturer which fabricated the contents of a label would doubtless take care to ensure that the stated components of its product added up to 100%. Therefore, proof of an understatement is likely to accompany proof of an overstatement, and will certainly imply the existence of one. Whether this is regarded as involving one or two violations of the law hardly seems to alter the gravity of the offense.

> the *percentage of the total fiber weight* of the wool product, exclusive of ornamentation not exceeding 5 per centum of said total fiber weight, of . . . (4) each fiber *other than wool if said* percentage by weight of such fiber is 5 per centum or more; . . . (emphasis added).

In our view the underlined words prescribe that each and every non-wool fiber in a wool product should be identified and its percentage given, if such fiber constitutes more than 5% of the product.

Marcus suggests that this requirement could be satisfied merely by designating all non-wool fibers together as "man-made" fibers, with their combined percentage stated. This interpretation, however, appears inconsistent with use of the word "each" in the statute.

Moreover, while Congress was apparently silent at the time of passage of the Wool Act as to what it intended to require by way of labeling of non-wool fibers (except for its express statement in the statute) its intent with respect to the earlier Act can be glimpsed by a consideration of the history of the Textile Act which the *Marcus* decision does not appear to address. In passing the Textile Act, Congress acted on the assumption that consumers would be interested in knowing the content of *all fibers* in covered products, without regard to superiority. Therefore, in language virtually identical to that employed in the above-quoted portion of the Wool Act, Congress required a listing in *non-wool* products of

> the percentage of each fiber present, by weight, in the total fiber content of the textile fiber product, exclusive of ornamentation not exceeding 5 per centum by weight of the total fiber content. . . .

[17] Congress undoubtedly excluded products "required to be labeled under the Wool Products Labeling Act of 1939" from its definition of products covered by the Textile Act because it presumed that the Wool Act already required virtually identical labeling requirements for non-wool fibers contained in wool products. That assumption does not appear unreasonable since the Wool Act would seem to have expressly so required.

Accordingly, it is our view that whatever omissions exist in the legislative history of the Wool Act as to how it should be construed with respect to non-wool products were answered when Congress passed the Textile Act. The concern of Congress with wool representations when it passed the Wool Act cannot be allowed to obscure the fact that in plain language it did establish a regulatory scheme to require percentage labeling of non-wool fibers, a scheme which was ultimately perfected in the Textile Act. As complaint counsel point out, the interpretation rendered in *Marcus* would defeat this statutory design. While a product with no wool must be labeled as to each constituent fiber under the Textile Act, a product with small amounts of wool becomes subject to the Wool Act (and exempt from the Textile Act) and thereby need not be labeled at all, even though the consumer's principal interest in the product will surely be with respect to non-wool fibers. In the instant case, actual misrepresentations of fiber content have occurred and as noted above we believe these are readily reached under Section 5. However, Section 5 is clearly not an adequate substitute for the careful Congressional design, because it lacks the same criminal and civil remedial provisions that are contained in the labeling laws. Moreover, it is not clear that a finding of "deception" under Section 5 alone could be properly applied to the unscrupulous manufacturer who simply included tiny quantities of wool in its fabric (thereby rendering it a product covered by the Wool Act) and thereafter proceeded to label it accurately "other non-wool fibers 99%," a formulation seemingly endorsed by the Second Court in *Marcus*.

For the foregoing reasons, the Commission remains persuaded of the view that the Wool Act applies to misbranding non-wool fibers in wool products, and requires accurate statements of the amount of each non-wool fiber which constitutes more than 5% by weight of the product. It is the Commission's respectful hope and desire that the Second Circuit, when faced with the compelling facts of this case or others like it, would reconsider its holding in the *Marcus* case in the respects indicated above. [18]

Synopsis of Determinations for 15 U.S.C. 45(m)(1)(B)

In order to facilitate application of the Commission's holdings in this case to others who may be engaged in the same practices as respondents, pursuant to the provisions of 15 U.S.C. 45(m)(1)(B) [(§205 of the Magnuson-Moss Act)], the Commission has determined to set forth in synopsis form a statement of the acts or practices determined to be unfair and deceptive in this proceeding:[15]

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[15] The Commission's decision to prepare a synopsis of its determinations in this case is undertaken in the exercise of its discretion, in order to simplify application of these determinations to other cases. Such a procedure is not required by 15 U.S.C. 45(m)(1)(B).

I. *Acts or Practices Which Are Unfair or Deceptive Pursuant to the Wool Products Labeling Act or the Textile Fiber Products Labeling Act, and Section 5 of the Federal Trade Commission Act*

1. It is an unfair and deceptive act or practice to falsely or deceptively stamp, tag, label, or otherwise identify wool products as to the character or amount of the constituent fibers which they contain.

2. It is an unfair and deceptive act or practice to fail to affix securely to, or to place on, a wool product a stamp, tag, label, or other means of identification showing in a clear and conspicuous manner the correct percentage of the total fiber weight of such wool product exclusive of ornamentation not exceeding five percent of said total fiber weight of (1) wool, (2) reprocessed wool, (3) reused wool, (4) each fiber other than wool when said percentage by weight of such fiber is five percent or more, and (5) the aggregate of all other fibers.

3. It is an unfair and deceptive act or practice (a) to falsify or fail to set forth upon invoices of imported wool products required by Section 484 of the Tariff Act of 1930, all information required by the Wool Products Labeling Act (15 U.S.C. 68) to be disclosed in connection with those products; and (b) to falsify or perjure the consignee's declaration provided for by Section 485 of the Tariff Act of June 17, 1930, insofar as it relates to the information required by the Wool Products Labeling Act to be disclosed in connection with wool products. [19]

4. It is an unfair and deceptive act or practice to falsely or deceptively stamp, tag, label, invoice, advertise, or otherwise identify any textile fiber product as to the name or amount of constituent fibers contained therein.

5. It is an unfair and deceptive act or practice to fail to affix to a textile fiber product a stamp, tag, label, or other means of identification showing in words and figures plainly legible the true percentage of each fiber present by its true generic name, if the weight of such fiber is 5 percent or more of the total weight of the product.

6. It is an unfair and deceptive act or practice (a) to falsify or fail to set forth upon invoices of imported textile fiber products required under Section 484 of the Tariff Act of 1930, all information required by the Textile Fiber Products Identification Act (15 U.S.C. 70) to be disclosed in connection with those products; and (b) to falsify or perjure the consignee's declaration required by Section 485 of the Tariff Act of 1930 insofar as it relates to the information required to

be disclosed by the Textile Fiber Products Identification Act to be disclosed in connection with textile fiber products.

II. *Acts or Practices Held To Be Unfair and Deceptive Pursuant to Section 5 of the Federal Trade Commission Act:*

1. It is an unfair and deceptive act or practice to misrepresent the amount by which a fabric will shrink when it is washed.
2. It is an unfair and deceptive act or practice to misrepresent the amount of constituent fibers contained in a wool or textile fiber product.

FINAL ORDER

This matter has been heard by the Commission upon the cross-appeals of complaint counsel and respondents' counsel from the initial decision and upon briefs and oral argument in support and in opposition to each appeal. The Commission, for the reasons stated in the accompanying Opinion, has granted the appeal of complaint counsel and denied the appeal of respondents' counsel. Therefore, [2]

It is ordered, That the initial decision of the administrative law judge be adopted as the Findings of Fact and Conclusions of Law of the Commission, except for p. 31 paragraph headed "Understatements of Fiber Content"; p. 35, line 7, sentence beginning "Still . . ." through line 29, sentence ending with "violation"; p. 47, first full paragraph onward.

Other Findings of Fact and Conclusions of Law of the Commission are contained in the accompanying Opinion.

It is further ordered, That the following order to cease and desist be entered:

ORDER

It is ordered, That respondents Verrazzano Trading Corporation, a corporation, Francesco Datini Inc., a corporation, Lanificio Tuscania Inc., a corporation, Lima Textiles Inc., a corporation, and Hudson Textile Corporation, a corporation, their successors and assigns and their officers, and Walter Banci, individually and as agent for said corporations, and as an officer of Lanificio Tuscania Inc. and Lima Textiles, Inc., and as a partner trading and doing business as Lanificio Walter Banci s.a.s., and respondents' representatives, agents and employees, directly or through any corporation, subsidiary, division, or any other device, in connection with the introduction, sale, advertising or offering for sale in commerce, or the transportation or causing to be transported in commerce, or the importation into the United States of any textile fiber product; or in connection with the sale, offering for sale, advertising, delivery, transportation, or causing to be transported, of any textile fiber product which has been advertised or offered for sale in commerce; or in connection with the sale, offering for sale, advertising, delivery, transportation or causing to be transported, after shipment in commerce of any textile fiber product, as the terms "commerce" and "textile fiber product" are defined in the Textile Fiber Products Identification Act, do forthwith cease and desist from misbranding such textile fiber products by: [3]

1. Falsely or deceptively stamping, tagging, labeling, invoicing, advertising or otherwise identifying such products as to the name or amount of constituent fibers contained therein.
2. Failing to affix a stamp, tag, label, or other means of identification to each such textile fiber product showing in a clear, legible and conspicuous manner each element of information required to be disclosed by Section 4(b) of the Textile Fiber Products Identification Act.

It is further ordered, That respondents Verrazzano Trading Corporation, a corporation, Francesco Datini Inc., a corporation, Lanificio Tuscania Inc., a corporation, Lima Textiles Inc., a corporation, and Hudson Textile Corporation, a corporation, their successors and assigns and their officers, and Walter Banci, individually and as agent for said corporations and as an officer of Lanificio Tuscania Inc. and Lima Textiles Inc. and as a partner trading and doing business as Lanificio Walter Banci s.a.s., and respondents' representatives, agents and employees, directly or through any corporation, subsidiary, division, or other device, do forthwith cease and desist from importing, or participating in the importation of, any textile fiber product into the United States except upon filing bond with the Secretary of the Treasury in a sum double the value of said products and any duty thereon, conditioned upon compliance with the provisions of the Textile Fiber Products Identification Act.

It is further ordered, That respondents Verrazzano Trading Corporation, a corporation, Francesco Datini Inc., a corporation, Lanificio Tuscania Inc., a corporation, Lima Textiles Inc., a corporation, and Hudson Textile Corporation, a corporation, their successors and assigns and their officers, and Walter Banci, individually and as agent for said corporations and as an officer of Lanificio Tuscania Inc. and Lima Textiles Inc., and as a partner trading and doing business as Lanificio Walter Banci s.a.s., and respondents' representatives, agents and employees, directly or through any corporation, subsidiary, division, or other device, in connection with the introduction into commerce, or the offering for sale, transportation, distribution, delivery for shipment or shipment in commerce of wool products, as "commerce" and "wool product" are defined in the Wool Products Labeling Act of 1939, do forthwith cease and desist from misbranding such products by: [4]

1. Falsely and deceptively stamping, tagging, labeling, or otherwise identifying such products as to the character or amount of the constituent fibers contained therein.

2. Failing to securely affix to or place on each such product a stamp, tag, label or other means of identification showing in a clear and conspicuous manner each element of information required to be disclosed by Section 4(a)(2) of the Wool Products Labeling Act of 1939.

It is further ordered, That respondents Verrazzano Trading Corporation, a corporation, Francesco Datini Inc., a corporation, Lanificio Tuscania Inc., a corporation, Lima Textiles Inc., a corporation, and Hudson Textile Corporation, a corporation, their successors and assigns and their officers, and Walter Banci, individually and as agent for said corporations and as an officer of Lanificio Tuscania Inc. and Lima Textiles Inc. and as a partner trading and doing business as Lanificio Walter Banci s.a.s., and respondents' representatives, agents and employees, directly or through any corporation, subsidiary, division, or other device, do forthwith cease and desist from importing or participating in the importation of wool products into the United States except upon filing bond with the Secretary of the Treasury in a sum double the value of said wool products and any duty thereon, conditioned upon compliance with the provisions of the Wool Products Labeling Act of 1939.

It is further ordered, That respondents Verrazzano Trading Corporation, a corporation, Francesco Datini Inc., a corporation, Lanificio Tuscania Inc., a corporation, Lima Textiles Inc., a corporation, and Hudson Textile Corporation, a corporation, their successors and assigns and their officers, and Walter Banci, individually and as agent for said corporations and as an officer of Lanificio Tuscania Inc. and Lima Textiles Inc. and as a partner trading and doing business as Lanificio Walter Banci s.a.s., and respondents' representatives, agents and employees, directly or through any corporate or other device, in connection with the importing, advertising, offering for sale, sale or distribution of wool and/or textile products, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from misrepresenting the character and amount of constituent fibers contained in such products and the shrinkage factor of such products on contracts, invoices, shipping memoranda or labels applicable thereto, or in any other manner. [5]

It is further ordered, That respondents deliver a copy of this order by registered mail to each of their customers that purchased qualities Sioux, Manito, Totem, Marnie, Gretel, Isabel, Veruska, Spluga, Eva, Navajo, Ellen, Ingrid or Myla during the period January 1, 1973 to June 24, 1975.

It is further ordered, That the individual respondent named herein promptly notify the Commission of the discontinuance of his present business or employment and his affiliation with a new business or employment. Such notice shall include said respondent's current business address and a statement as to the nature of the business or employment in which he is engaged, as well as a description of his duties and responsibilities.

It is further ordered, That the corporate respondents shall forthwith distribute a copy of this order to each of their operating divisions and/or subsidiaries.

It is further ordered, That the corporate respondents notify the Commission at least thirty (30) days prior to any proposed change in said respondents such as dissolution, assignment, or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporations which may affect compliance obligations arising out of the order.

It is further ordered, That respondents herein shall within sixty (60) days after service upon them of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied with this order.

IN THE MATTER OF

KOSCOT INTERPLANETARY, INC., ET AL.

Docket 8888. Interlocutory Order, May 16, 1978

Order denying petition for reconsideration on finding that respondents failed to show the existence of circumstances which would warrant reopening or reconsidering the docketed proceeding.

ORDER DENYING "PETITIONS FOR RECONSIDERATION"

The Court of Appeals, by order of December 28, 1977, granted leave to two respondents in *Koscot Interplanetary, Inc., et al.,* Dkt. 8888, 86 F.T.C. 1106 (1975), to apply to the Commission for reconsideration of that proceeding based on further defenses or additional evidence.[1] Having carefully considered the contentions raised by respondents Glenn W. Turner and Raleigh P. Mann in petitions filed April 14, 1978,[2] and the answering submission of complaint counsel, the Commission hereby denies the petitions and directs that the Court of Appeals be notified that the Commission will not request the Court to remand the record for further proceedings. The Commission finds that respondents have failed to show the existence of circumstances which would warrant reopening or reconsidering the docketed proceeding.

In so holding, the Commission takes note of the exhaustive nature of the proceedings in *Koscot,* which stretched from May 24, 1972, when complaint issued, through the filing of the initial decision on March 20, 1975, to the issuance of the Commission's decision and order on November 18, 1975, and subsequent modifying order on January 13, 1976 [87 F.T.C. 75]. The trial spawned a transcript in excess of 5000 pages, accompanied by numerous documents. Respondents received a proper hearing on the record, with notice and a fair opportunity to be heard, to be represented by counsel, to conduct cross-examination, and to offer rebuttal evidence. See 5 U.S.C. 554, 556, 557; 15 U.S.C. 45.

Moreover, they exercised their rights. Respondent Turner had counsel of record throughout the entire proceeding and at no time objected to the competency or adequacy of such counsel. Respondent

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[1] The Court also gave permission to respondents to petition the Commission for appointment of counsel, upon a proper showing of indigency. They have made no such motion and are represented in this matter by retained counsel.

[2] The following abbreviations are used in this order:

Turner petition - Petition by respondent, Glenn W. Turner, for Reconsideration
Mann petition - Petition by respondent, Raleigh P. Mann, for Reconsideration
C.C. Answer - Complaint Counsel's Answer to above Petitions
ALJ - Administrative Law Judge

Mann had legal representation during parts of the adjudication, including, contrary to his statement, the period "during the very critical post-hearing proceedings." Mann petition at 4. Notice of Appeal of Administrative Law Judge's Initial Decision filed May 29, 1975, see Appendix A to C.C.'s Answer, point 49. Complaint counsel has sworn that he timely advised respondent Mann of the availability of appointed counsel for indigents, but petitioner Mann declined to pursue this option. See Appendix D to C.C. Answer.[3] Mann testified on the record and presented all the evidence which the instant petition seeks to reassert. At that time he was afforded the right to make a statement on his own behalf for the record, and did so. See Mann petition at 9. A month later, respondent Mann filed, *pro se,* a motion to dismiss, which was denied in the initial decision. 86 F.T.C. at 1127. He was, however, excepted from the requirements of the ALJ's restitution order, at least partly on the basis of his testimony. 86 F.T.C. at 1155. Counsel for respondent Turner filed a Brief in Opposition to Complaint Counsel's Proposed Findings of Fact. The same counsel filed an Appeal Brief and argued the cause for *all* respondents before the Commission. While the Commission affirmed most aspects of the initial decision, it excised the order provisions requiring restitution, which objective was the main focus of respondents' counsel's argument on appeal to the Commission.

Respondents now contest the order on the ground of inadequacy of representation. They claim that insufficiency in representation, which was not visited upon them by any act of the Commission, led to a failure to offer exculpatory evidence. Respondents have not, however, actually presented any additional or "newly discovered" evidence, see *Smith* v. *Pollin,* 194 F.2d 349, 350 (D.C. Cir. 1952), and content themselves with restating their desire for further proceedings which appear to hold only the promise of reviewing old evidence. Respondent Mann offers nothing more than a reiteration of matters already in the record, which were the subject of findings by the ALJ and of a denial of Mann's motion to dismiss. Mann petition at 5-8. That respondent now believes a more articulate presentation or more cogent marshalling of his arguments would have exonerated or might still vindicate him cannot be the basis of reopening and further protracting proceedings where the evidence was already fully considered, and with benefit to respondent. The doctrine of *res judicata* is not without purpose. Cases cannot be reheard whenever respondents find a better orator or a superior way to package their contentions. There is an interest in finality, and in preserving scarce public resources. Care must be taken to protect the public interest, and the rights of those who fall victim to the few who would violate the law.

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[3] Even without notice of the Commission's policy of appointing counsel, it would seem a logical request for an indigent respondent to make *sua sponte.*

It is understandable that respondent Mann now regrets his failure to present a defense on the merits, but such was his choice, and one echoed by others who had the benefit of counsel throughout (including Koscot itself, which even respondent Turner does not allege was inadequately represented). Mann's petition reaffirms that he believed his testimony and documentary evidence were sufficient to absolve him of liability for any violations of law. Mann petition at 9-10. This was a strategic decision made in presenting his case and connot be undone because the ALJ and Commission were not persuaded to his view. Respondent Mann suffered no denial of rights incident to a fair hearing.

Respondent Turner claimed before the Court of Appeals and now here that his legal representation fell short of the mark because his counsel appeared on behalf of multiple parties, subjecting respondent to a conflict of interest which prejudiced him since "certain evidence tending to disprove the allegations against [him] was not proffered." Court of Appeals Order of December 28, 1977. See Turner petition at 5–7. To support this contention, he offers only a conclusory, *ex post facto* affidavit of his former counsel which appears to contradict earlier statements made by that attorney on the adjudicative record, that there was no conflict of interest. See Appendix B to C.C. Answer, transcript at 4326-27.[4] Even assuming that respondent did not waive, either formally or constructively, objection to a possible conflict of interest, he points to no evidence which was omitted from the adjudication because of a real or theoretical conflict. Instead, he relies on a theory of diminished vigor, that is, that counsel slighted the case for Turner to concentrate on that of Koscot, the client for which he received some compensation.[5] There is no evidence that this occurred to any noticeable degree, and considering that Turner was found to be the alter ego of Koscot (86 F.T.C. at 1123) a radical divergence of interests appears unlikely.

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[4] Cannon 5 of the Code of Professional Responsibility and attendant Ethical Considerations and Disciplinary Rules plainly warn against the representation or continued representation of multiple clients where a conflict of interest may occur. See especially EC5–14 to EC5–19 and DR5–105. Respondent's counsel specifically represented that he was familiar with Canon 5 and was not in violation of it. He admitted of the potential for conflict between respondents if less than all wished to effect a consent agreement, but this situation did not develop. He adverted to a "conflict of itself [sic] between Mr. Wilder and Mr. Bunting," transcript at 4325, but not to any involving Mr. Turner. He also used the word "conflict" in a looser sense, in saying "But quite realistically, there is a conflict. If they had each [the individual respondents] had money and had their druthers, I think each of them would have had a different attorney representing them in all kinds of litigation across the country, but circumstances were that they were stuck with one law firm for which they pay no money." Transcript at 4326. It is not clear which meaning is intended by Mr. Robinson's affidavit, see Exhibit I to Turner petition and also p. 6 of the petition. Moreover, the affidavit indicates that any conflict affecting Glenn Turner could only have arisen after the "early August 1974" sale of Koscot. Affidavit at 4. In fact, the sale occurred in August 1973, according to the ALJ's findings, 86 F.T.C. at 1121. Mr. Robinson's averment on the record of the absence of a conflict of interest took place on August 19, 1974, and any conflicts triggered by the sale would presumably have come to light by the time Mr. Robinson denied that any existed.

Complaint counsel has pointed out other inconsistencies in this affidavit which must erode its credibility. C.C. Answer at 8–9. One of the most serious is prior counsel's implication in the 1976 affidavit that he repeatedly tried to withdraw his representation on the ground of conflict of interest. See Turner petition at 6, point 3. His motion to withdraw, attached as Exhibit D to the Turner petition does not plead conflict of interest as a supporting basis. See C.C. Answer at 6–7.

To show prejudice, respondent states that no defense on the merits was presented on his behalf, that "virtually all of the relatively few . . . items of documentary evidence submitted on behalf of respondents were related to the interest of Respondent Koscot," and that "the principal post-hearing filings on behalf of respondents . . . only tangentially, and with minimal efficacy, tended to protect, advance, or defend the significant interests of Respondent Turner." Turner petition at 5–6. The ALJ found, however, that no real defense on the merits was presented on behalf of Koscot either, since none of the respondents represented by attorney Robinson objected to the issuance of the order proposed by complaint counsel except with regard to restitution. 86 F.T.C. at 1118–19, 1178. The documentary evidence introduced for respondents accordingly went to the contested restitution issue, "primarily relating to the status of respondent Koscot as a result of its petition for an arrangement under Chapter 11 of the Federal Bankruptcy Act," 86 F.T.C. at 1118. As the other respondents had refused to discuss their finances, standing on their Fifth Amendment rights (86 F.T.C. at 1183), there were not many disputed issues about which respondents could have submitted documentary evidence. With regard to the post-hearing filings, the Commission can detect little difference in the force and persuasiveness of the arguments for the various respondents. Respondent Turner concedes that the Brief in Opposition and Appeal Brief "ostensibly" defended the interests of all the respondents counsel represented. Turner petition at 5. He offers no clue as to what, if anything, negated this appearance of representation of all the parties' interests. Counsel seems to have made a tactical decision that only the restitution issue should be pursued, and his arguments would seem to have benefited all the respondents. Indeed, there is ample evidence that respondents were willing from the start to agree to an order very like the one the Commission ultimately adopted and only really opposed the restitution remedy. See Appendix A to C.C. Answer, points 4–5, 32–34. Particularly as the Commission dropped the restitution provisions from its order, we agree with complaint counsel that "it simply cannot be said that prior counsel did not defend the significant interests of petitioner." C.C. Answer at 12.

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[5] In any case, it appears that the representation of Koscot had not proved so lucrative for Mr. Robinson that it would likely have induced him to abandon the other respondents in Koscot's favor, to the extent that their interests may have differed. Compare Turner petition at 6, point 2, with transcript at 5098, 5104–05, and respondents' "Response Complaint Counsel's Answer to Motion for Extension of Time," cited in Appendix A TO C.C. Answer, points 30, 52. The performance of special bankruptcy counsel for Koscot, and any particularized assistance he gave to Koscot is not relevant to the charge of deficient representation originating in Mr. Robinson's alleged conflict of interest.

It should also be noted that "none of the respondents put on an individual defense in the Jacksonville mail fraud trial either," (transcript at 5117, quoted in C.C. Answer at 11), which ended in a hung jury. Mr. Robinson's decision to follow the same course before the Commission may well have reflected a tactical judgment based upon his experience. Courts do "not sit to second guess strategic and tactical choices made by trial counsel." *United States* v. *DeCoster*, 487 F.2d 1197, 1201 (D.C. Cir. 1973).

Most important is the fact that the record shows, and respondent has not demonstrated otherwise, that the actions counsel did not take, the witnesses he did not call, the exhibits he did not introduce, and the case he did not make, derived from strategic decisions or possibly lack of funds[6] and not from any conflict of interest respondent here argues prevented the proffering of exculpatory evidence. Nor has respondent offered any additional evidence to contradict the record on this point. Respondent Turner has failed to show the existence of a conflict of interest or that any prejudice has accrued to him from what he mistakenly perceives to be a possible conflict. Especially in a civil case, where the application and policy of the Sixth Amendment are unclear, see *United States* v. *Rogers*, 534 F.2d 1134, 1135 (5th Cir.), *cert. denied*, 429 U.S. 940 (1976), the courts do not lightly assume the inadequacy of counsel. *United States* v. *McCord*, 509 F.2d 334, 353 (D.C. Cir. 1974), *en banc*, *cert. denied*, 421 U.S. 930 (1975).

Respondent Turner raises another issue, collateral to those directed for Commission consideration by the Court. He argues that the assertion of their privilege against self-incrimination prevented him and the other respondents from testifying and therein exonerating some or all of the respondents from liability. Turner petition at 7. Even though respondents did not request immunity, Mr. Turner contends that the Commission's failure to secure it for respondents under Section 4.12 of the Rules kept him from participating "actively and directly in the proceedings without the necessary intervention of unwilling, and consequently ineffective, counsel." Turner petition at 8. To the extent that this represents an assertion that conducting one's case *pro se* is impossible for those who seek to preserve their Fifth Amendment rights, it is mistaken. Only by voluntarily testifying on the stand and only in response to questions related to incriminating matters, would he have risked waiver of the privilege.

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[6] Although counsel for respondents hinted several times during the proceeding that some or all of them were in straitened circumstances, respondents refused to give evidence on the question, citing the privilege against self-incrimination, and thus no related findings were made. 86 F.T.C. at 1183. Accordingly, it is not known whether their failure to fund their attorney was a matter of choice or necessity.

8 Wigmore, Evidence §2276 (McNaughton rev. 1961). Respondent did not need immunity to examine or cross-examine witnesses or to submit evidence on his own behalf. Had he wished to introduce his own testimony, which was evidently not needed by complaint counsel, respondent could himself have sought immunity by applying to the ALJ under Section 4.12.[7] The same procedure could have secured for him the immunized testimony of other respondents. Respondent Turner made no effort during the proceeding to avail himself of the immunity provision and now claims that he was prejudiced in his case because complaint counsel did not do so for him. Turner petition at 8. But complaint counsel had no such duty. It is no abuse of the right against self-incrimination to respect its privilege of silence.

Respondent Turner now seeks to turn that shield into a sword (cf. *United States* v. *Newman*, 468 F.2d 791 (5th Cir. 1972), *cert. denied*, 411 U.S. 905 (1973)), by claiming a right to additional hearings where undescribed testimony of co-respondents may be elicited, if they are willing, now that the criminal charges against them have been resolved. Turner petition at 7. Respondent Turner himself would like another chance to testify. He supplies no information, however, upon which to judge the likelihood or value of this possible testimony. Nor does he address the fact that respondents had already pleaded *nolo contendere* before the oral argument[8] and thus could have sought leave to give their testimony even before the Commission reviewed the initial decision and issued its opinion and final order. He would have us remand for new hearings on the strength of a vague intimation that further evidence may be forthcoming and, if so, that it may be valuable. Turner petition at 7. He does not even assert that this hypothetical evidence would change the outcome of the proceedings. Under the circumstances, the Commission does not find it unduly harsh or in any was contrary to the public interest to reject this gambit. "A respondent cannot be permitted to gamble on one course of action and, upon an unfavorable decision, to try another course of action." *Gross* v. *SEC*, 418 F.2d 108, 109 (2d Cir. 1969).

The capacity of the administrative process to resolve cases will be seriously compromised, and the public badly disserved,[9] if respon-

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[7] The Commission has made no determination that immunity would or should have been granted in this case. See, *e.g.*, *United States* v. *Bautista*, 509 F.2d 675, 677 (9th Cir.), *cert. denied sub nom. Monsivais* v. *United States*, 421 U.S. 976 (1975); *Earl* v. *United States*, 361 F.2d 531, 534 (D.C. Cir. 1966), *cert. denied*, 388 U.S. 921 (1967).

[8] Indeed, their counsel was directly asked about the status of the criminal proceedings during oral argument before the Commission and revealed their conclusion. Transcript of Oral Argument, October 2, 1975, at 14-15.

[9] We do feel compelled to note that the lengthy trial record presented to the Commission in this matter, analyzed in depth in the ALJ's initial decision, and summarized in the Commission's opinion, reveals violations of 15 U.S.C. 45 and losses to the public of enormous proportions. Unless and until the Commission's order in this matter becomes final against respondents, they remain free to repeat the practices which contributed to those losses, without the strong deterrence which an order to cease and desist provides. Given that no evidence has been

(Continued)

dents in such cases are permitted to delay their finality for long periods of time by waiting for the conclusion of the administrative process and then hinting at the existence of further relevant evidence which might, in any event, have been presented at trial.

Having thoroughly and carefully considered the submissions of petitioners and complaint counsel, the Commission has determined that they do not raise any grounds that would warrant reconsideration by the Commission of its earlier decision, and therefore the Commission does not request that the Court of Appeals remand this matter to it for further proceedings. Accordingly,

It is ordered, That the "Petitions for Reconsideration" by respondents Mann and Turner are hereby denied.

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adduced to warrant reopening of administrative proceedings, the Commission is distressed that 2 1/2 years should have elapsed since the issuance of its order, without its consideration on the merits. The Commission is hopeful that this proceeding may be brought to a speedy conclusion and the public given the protection which the record indicates it deserves.

IN THE MATTER OF

KOSCOT INTERPLANETARY, INC., ET AL.

Docket 8888. Interlocutory Order, May 16, 1978

Grant of complaint counsel's motion requesting leave to file an answer to petition for reconsideration.

ORDER GRANTING LEAVE TO FILE ANSWER

Counsel supporting the complaint in this matter have filed two requests for brief extensions of time within which to file an answer to "Petitions for Reconsideration" filed by respondents Glenn W. Turner and Raleigh P. Mann pursuant to an order entered December 28, 1977 by the United States Court of Appeals for the District of Columbia. Complaint counsel, having received no response to these motions, subsequently filed an "Answer" accompanied by a motion to file the answer "out of time."

Complaint counsel have apparently assumed that the time established for filing of an answer is governed by Section 3.55 of the Commission's Rules of Practice, pertaining to requests for reconsideration of Commission orders. This section of the Rules requires that petitions for reconsideration be filed within 20 days after service of a Commission order. Thereafter, opposing counsel are given 10 days within which to file an answer. The Commission doubts whether Section 3.55 should properly be applied to the case at hand, because it plainly applies only to requests for reconsideration filed within a short time of the entry of an order, before the matter has left the Commission's jurisdiction.

Complaint counsel's position doubtless results from the use by petitioners and the Court of Appeals of the term "reconsideration" to characterize petitioners' request. Petitioners have also referred to Section 3.55 of the Rules. Assuming *arguendo* that this section of the Rules has any applicability to the matter at hand, the Commission has determined that the 8 days' total extension of time requested by complaint counsel is appropriate, given that respondents have had a much longer period of time than that allowed by Section 3.55 of the Rules within which to prepare the petition to which complaint counsel responds. Accordingly,

It is ordered, That complaint counsel's motion requesting leave to file an Answer to Respondents' Petitions for Reconsideration be granted.

IN THE MATTER OF

HERBERT R. GIBSON, SR., ET AL.

Docket 9016. Interlocutory Order, May 18, 1978

Request for subpoena enforcement denied without prejudice to renew.

ORDER DENYING REQUEST FOR SUBPOENA ENFORCEMENT WITHOUT PREJUDICE TO RENEW

On April 20, 1978, the administrative law judge, pursuant to Commission Rule 3.22 certified complaint counsel's Request for Court Enforcement of the Subpoena Served on Commission Witness Nix. For the reasons discussed below, we deny complaint counsel's request without prejudice to renewal at a later date.

The subpoena in question was dated March 16, 1978, served on Mr. Nix on March 22, 1978, with a return date of April 11, 1978. On April 10, 1978, complaint counsel received a letter from Mr. Nix indicating that he would not be able to comply with the subpoena because of illness. Attached to his letter is a statement to that effect from his physician, Dr. William deVlaming. Additionally, Mr. Nix indicated that he could not remember much of the information about which he spoke with complaint counsel and remarked on the fact that complaint counsel had previously indicated that he would not be called to testify.

Complaint counsel takes issue with each of Mr. Nix's assertions and points out that "failing memory is not a valid basis for failing to appear." Moreover, complaint counsel argues that the testimony of Mr. Nix

> is crucial for several reasons. He is one of the few witnesses that will testify as to the issues raised under Count III of the Complaint. His testimony is expected to directly contradict the testimony previously presented by respondent, Gerald P. Gibson. His testimony is finally expected to link respondents, H.R. Gibson Sr., H.R. Gibson, Jr. and Gerald P. Gibson, to payments and receipt of illegal brokerage.

Nevertheless, the administrative law judge has recommended that the request be denied because of the length of time that may be involved in an enforcement proceeding and because of the likelihood that no substantive evidence will be elicited if Mr. Nix cannot recall the events in question. At the same time, the administrative law judge notes that Mr. Nix could possibly be a "crucial witness on whom complaint counsel placed considerable reliance."

We have determined that the best way to reconcile the needs of all parties is to deny without prejudice, complaint counsel's request with instructions that the administrative law judge and the parties consider the procedures of Commission Rule 3.33. Rule 3.33(a) provides that:

At any time during the course of a proceeding . . . the Administrative Law Judge, in his discretion, may order the taking of a deposition and the production of documents by the deponent.

Furthermore, Section 3.33(f) provides for the introduction into evidence of a deposition if the administrative law judge finds "that the deponent is unable to attend or testify because of age, sickness, infirmity or imprisonment."

In this way, Mr. Nix will not be removed from the care and supervision of his doctor, or otherwise inconvenienced to the possible detriment of his health.[1] Moreover, complaint counsel will have the benefit of whatever recollection Mr. Nix can bring to bear on the situation, and Mr. Nix's memory lapses will be duly noted on the record under oath.

By its action today, the Commission should not be seen as invalidating the outstanding subpoena against Mr. Nix. The procedure suggested is an alternative to lengthy enforcement proceedings and at the same time adheres to the needs of Mr. Nix. Whether enforcement proceedings will ultimately be required as to the presently outstanding subpoena we have no way of knowing. Nevertheless, complaint counsel will not be prejudiced in renewing the request if it is determined that Section 3.33 is not feasible or if Mr. Nix again refuses to comply. Accordingly,

It is ordered, That complaint counsel's Request for Court Enforcement of the Subpoena Served on Commission Witness Nix be, and the same hereby is, denied without prejudice to renewal at a later date;

It is further ordered, That the parties and the administrative law judge consider proceedings pursuant to Commission Rule 3.33.

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[1] **Apparently, Mr. Nix is not completely incapacitated by his illness as we note that on April 7th he was said to be playing golf.**

IN THE MATTER OF
SAFEWAY STORES, INCORPORATED

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket 9053. Complaint, Sept. 3, 1975—Decision, May 18, 1978

This consent order, among other things, requires an Oakland, Calif. retail food store chain to cease over-pricemarking and failing to sell advertised items at or below advertised prices. Further, food stores are required to conspicuously post advertisements and notices encouraging customers to check prices of advertised items. The order additionally obligates the firm to maintain business records for a period of three years, and to establish a surveillance program designed to ensure compliance with the terms of the order.

Appearances

For the Commission: *Robert Eliot Easton, Sr.* and *James J. Angelone.*

For the respondent: *James F. Rill, Collier, Shannon, Rill, Edwards & Scott,* Washington, D.C.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Safeway Stores, Inc., a corporation, hereinafter sometimes referred to as respondent, has violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereto would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

COUNT I

(Alleging violations of Section 5 of the Federal Trade Commission Act.)

PARAGRAPH 1. Respondent, Safeway Stores, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Maryland with its office and principal place of business located at 4th and Jackson Sts., Oakland, California.

PAR. 2. Respondent is engaged in the operation of a chain of retail food stores, operating approximately 1950 stores in 27 states and the District of Columbia. Its volume of business is substantial, totalling approximately 6.77 billion dollars in retail food sales in 1973. In the operation of its retail food stores, respondent offers and sells to its customers an extensive line of groceries and other merchandise, including food, drugs, cosmetics and devices as those terms are defined in the Federal Trade Commission Act, all of which are sometimes referred to hereinafter as "items." Some of said items are manufactured or processed by respondent at its manufacturing and processing plants located in various states. However, many of said items are purchased from numerous independent suppliers located throughout the United States.

PAR. 3. In the course and conduct of its business, respondent now causes, and for some time last past has caused, directly or indirectly, the aforesaid items to be shipped and distributed from its manufacturing and processing plants or from its other sources of supply to its warehouses, distribution centers, or retail food stores located in various states other than the state or origination, distribution or storage of said items. In the further course and conduct of its business, respondent transmits contracts, business correspondence, monies and other documents from its stores, offices, and divisions located in states other than the states in which such contracts, correspondence, monies and other documents originated. Respondent maintains, and at all times mentioned herein has maintained, a substantial course of trade in the distribution, advertising, offering for sale, and sale of the items described in Paragraph Two, in commerce, as "commerce" is defined in the Federal Trade Commission Act.

PAR. 4. In the course and conduct of its business, and for some time last past, respondent has been and is now disseminating, and causing the dissemination of, certain advertisements concerning the said items by various means in commerce, as "commerce" is defined in the Federal Trade Commission Act, including but not limited to, advertisements in newspapers of general and interstate circulation and other advertising media, for the purpose of inducing and which were likely to induce, directly or indirectly, the purchase of said items from responent; and respondent has been and is now disseminating, and causing the dissemination of, advertisements concerning said items by various means, including but not limited to the aforesaid media, for the purpose of inducing and which were likely to induce, directly or indirectly, the attempted or actual purchase from respondent of the said items in commerce, as "commerce" is defined in the Federal Trade Commission Act. Many of those advertisements list or depict the said items and also contain statements and representations concerning the price or terms at which said items would be offered for sale. Many of the aforesaid advertisements contain further direct and express statements and representations concerning the time periods during which the offers would be in effect and the locations of respondent's food stores at which the offers would be made.

Par. 5. Through the use of such advertisements disseminated in various areas of the United States served by respondent's retail food stores, respondent has represented, directly or by implication, that in those stores covered by such advertisements, during the effective periods of the advertised offers, the items listed or depicted in such advertisements would be sold to persons who attempted to purchase such items at prices at or below the advertised prices for such items.

Par. 6. In truth and in fact, in a significant number of respondent's retail food stores covered by such advertisements, during the effective periods of the advertised offers, certain numbers of items listed or depicted in the said advertisements were marked with prices higher than the advertised prices, and, as a result, a substantial number of items marked with a higher price were sold to persons who purchased such items at prices higher than the advertised prices. Therefore, the statements and representations as referred to herein, were false, misleading and deceptive.

Par. 7. By disseminating or causing the dissemination of advertisements which offer or present for sale items at specific prices, by permitting the units of certain numbers of said items to remain marked with prices higher than the advertised prices and by selling a substantial number of items so marked to customers at prices higher than the advertised prices, during the effective periods of such advertised offers at a significant number of stores covered by said advertisements, respondent has been and now is engaged in unfair acts and practices.

Par. 8. In the course and conduct of its business, and at all times referred to herein, respondent has been and now is in substantial competition in commerce, with corporations, partnerships, firms and individuals in the retail food and grocery business.

Par. 9. The use by respondent of the aforesaid unfair and false, misleading and deceptive statements, representations, acts and practices has had and now has the capacity and tendency to mislead members of the purchasing public into the erroneous and mistaken belief that the said statements and representations were and are true, and to induce such persons to go to respondent's stores and to purchase from respondent substantial quantities of the advertised items at prices in excess of the advertised prices.

Par. 10. The acts and practices as aforesaid were and are all to the prejudice and injury of the public and of respondent's competitors and constituted and now constitute unfair methods of competition in commerce and unfair or deceptive acts or practices in commerce in violation of Section 5 of the Federal Trade Commission Act.

COUNT II

(Alleging violations of the Federal Trade Commission Trade Regulation Rule Concerning Retail Food Store Advertising and Marketing Practices (16 C.F.R. 424), and Section 5 of the Federal Trade Commission Act, the allegations of Paragraphs One, Two, Three, Four, and Eight; respectively, of Count I hereof are incorporated by reference in Count II as if fully set forth verbatim.)

PAR. 11. The Federal Trade Commission, pursuant to the Federal Trade Commission Act, as amended, 15 U.S.C. 41, *et seq.*, and the provisions of Subpart B, Part 1, of the Commission's Procedures and Rules of Practice, 16 C.F.R. 1.11, *et seq.*, conducted a proceeding for the promulgation of a trade regulation rule regarding retail food store advertising and marketing practices. Notice of this proceeding, including a proposed rule, was published in the Federal Register on November 14, 1969 (34 FR 18252). Interested parties were thereafter afforded opportunity to participate in the proceeding through the submission of written data, views and arguments, and to appear and orally express their views as to the proposed rule and to suggest amendments, revisions, and additions thereto.

The Commission considered all relevant matters of fact, law, policy, and discretion, including the data, views, and arguments presented on the record by interested parties in response to the Notice as indicated in the accompanying Statement of Basis and Purpose (36 FR 8777 (May 13, 1971)) and as prescribed by law, determined that the adoption of the trade regulation rule was in the public interest, and, accordingly, promulgated the Trade Regulation Rule Concerning Retail Food Store Advertising and Marketing Practices on May 13, 1971, effective July 12, 1971.

PAR. 12. Respondent is a member of the retail food store industry, and its acts and practices in connection with the sale and offering for sale of food and grocery products or other merchandise subject to the jurisdiction of Section 5 of the Federal Trade Commission Act are within the intent and meaning of, and are subject to, the provisions of the aforesaid Trade Regulation Rule.

PAR. 13. In connection with its advertisements disseminated as aforesaid, respondent, in a substantial number of instances, has failed to comply with Paragraph (2) of the Trade Regulation Rule by offering products for sale at stated prices by means of advertisements disseminated in areas served by certain of its stores which are covered by such advertisements and by failing in those stores to charge out to persons who attempted to purchase such items, substantial numbers of such advertised products at prices at or below the advertised prices during the effective periods of the advertisements, thereby failing to make said advertised items conspicuously and readily available for sale at or below the advertised prices.

PAR. 14. Respondent's aforesaid violations of the Trade Regulation Rule Concerning Retail Food Store Advertising and Marketing Practices constitute unfair methods of competition and unfair or deceptive acts or practices violative of Section 5 of the Federal Trade Commission Act.

DECISION AND ORDER

The Federal Trade Commission having issued a complaint based upon alleged acts and practices of Safeway Stores, Incorporated, a corporation, also trading and doing business as Safeway, hereinafter referred to as respondent, and having served such complaint upon respondent and having withdrawn the proceeding from adjudication based upon a joint motion for withdrawal from adjudication filed by complaint counsel and counsel for respondent; and

The respondent and counsel for the Commission having executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law had been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed pursuant to Sections 2.34 and 3.25 of its Rules, now in further conformity with the procedure prescribed in Section 3.25 of its Rules, the Commission hereby makes the following jurisdictional findings, and enters the following order:

1. Safeway Stores, Incorporated is a corporation organized, existing and doing business under and by virtue of the laws of the State of Maryland with its office and principal place of business located at 4th and Jackson Sts., Oakland, California.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

DEFINITIONS

"Retail Food Store" means any of respondent's stores within the United States engaged primarily in the sale of foods for home consumption, excluding convenience-type stores with less than 4,000 square feet of building area.

"Item" means any article of merchandise which differs from any other article as to commodity, product, brand, variety, style or form, grade, type of package or label, size or weight, provided, that size or weight is to be disregarded with respect to articles priced by a standard measure of weight or count.

"Scanned Item" means an item bearing a symbol, printed on or affixed to the packaging or container of such item, in any store in which it is electronically scanned by equipment which identifies and prints on a cash register tape the price of that item.

"Unit" means one consumer package of a packaged item or the smallest advertised quantity that a consumer may purchase of an unpackaged item, provided, for that purpose of paragraph I.A. (2) of the order, a unit of a multiple priced item (*e.g.*, three for 41 cents) shall consist of that quantity, count or weight to which the multiple price applies.

"Over-pricemarked Items" means an advertised item of which more than five (or in the event a display contains fewer than 20 units, more than one-fourth) of the units in any one display bear a marked price higher than the advertised price.

"Unmarked Item" means an advertised item of which no more than five (or in the event a display contains fewer than 20 units, not more than one-fourth) of the units in any one display are legibly marked with a price.

"Overcharged Item" means an over-pricemarked item or an unmarked item of which one or more units are charged out at higher than the advertised price.

"Survey" means a compliance survey conducted by or under the direction of the Federal Trade Commission of a sample of 50 or more retail food stores over a period of at least three different weeks with approximately equal numbers of stores surveyed during each week stores are surveyed. All store surveying shall be completed within a period of time not exceeding eight consecutive weeks. Stores to be surveyed shall be selected from at least three different Standard Metropolitan Statistical Areas (SMASs) with an approximately equal number of stores surveyed in each SMSA in which stores are surveyed. Stores to be surveyed shall be chosen in a manner which is consistent with this definition, but which is otherwise to be determined at the discretion of the staff or the Commission. Respondent waives any rights it might have to challenge the admissibility into evidence of the results of the survey of the sample on the grounds that those results are not projectable to a universe greater than the sample. Respondent, however, retains the right to challenge the evidentiary weight to be given to or inferences to be drawn from the results of any such survey on any legally available basis. All data collected in the course of a survey are to be recorded.

ORDER

PROHIBITED PRACTICES

I. *It is ordered*, That respondent Safeway Stores, Incorporated, a corporation, its successors or assigns, its officers, agents, representatives and employees, directly or through any corporation, subsidiary, division or other device, in connection with the advertising, offering for sale, sale or distribution of items offered or sold in its retail food stores, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from, directly or indirectly:

A. Disseminating, or causing dissemination of, any advertisement by any means which offers or presents any items for sale at a stated price, unless throughout the effective period of the advertised offer, at each retail food store covered by the advertisement:

(1) each unit of each such advertised item, any of which are marked with a price, is individually, clearly and conspicuously marked with a price no higher than the advertised price; provided that in the case of overpricemarked scanned items, clear and conspicuous posting of the advertised price of such items at the point of display will be deemed compliance with this requirement; and

(2) each unit of each such advertised item is charged out to customers at or below the advertised price; provided that in the case of advertised items the ultimate price of whose units are determined by the total dollar amount of the customer's order or the use of a coupon, or other similar conditional price arrangement, the prices at which the units are sold, and not the prices marked on the units, shall govern.

Provided further, it shall constitute a defense of a charge of overpricemarking or overcharging if respondent can show that such overpricemarking or overcharging was due to circumstances beyond respondent's reasonable control. It will be presumed that any instance of over-pricemarking or overcharging found was due to circumstances beyond respondent's reasonable control if respondent can show that such over-pricemarking and overcharging occurred despite respondent's reasonable procedures to eliminate all over-pricemarking and overcharging, and that upon learning of any specific instance or instances of such over-pricemarking or overcharging, respondent immediately acted to eliminate them and took reasonable measures to assure that they did not recur.

For respondent's procedures to be reasonable, respondent shall have the burden of establishing that:

(i) it has a reasonable basis in fact for concluding that its procedures for pricemarking and charging out advertised items are properly designed to achieve compliance with this order;

(ii) it has in effect a continuing surveillance program adequate to reveal whether its retail food stores are conforming with this order; and

(iii) respondent regularly conducts a review and analysis of results of the surveillance program adequate to determine whether changes in market conditions, technology or other changes make it necessary for respondent to revise its procedures for pricemarking and charging out advertised items to maintain compliance with this order.

II. A. No enforcement action will be brought against respondent for any alleged instances of overpricemarking or overcharging on the basis of a survey unless Respondent is notified in writing within three months following the completion of that survey that the survey has been conducted. At the time of said notice the Commission shall furnish respondent copies of written instructions to the persons making in-store observations, and sufficient documentary material that will reasonably enable Respondent to identify the stores, items and prices surveyed.

B. If, in any enforcement action brought against respondent, the Commission offers evidence purporting to establish an over-pricemarking rate for respondent, such rate shall be calculated by taking, as of the date(s) of any survey and for the stores selected, the total number of items over-pricemarked as a percent of the total number of advertised items than in effect for those stores.

III. *It is further ordered*, That throughout the effective period of such newspaper advertisement, respondent shall post conspicuously at or near each doorway affording entrance to the public of each retail food store,

(a) copy of the advertisement effective for that store; and

(b) the following statement:

Notice to Our Customers

To assure correct charging of advertised prices please check the price of any

advertised item you purchase against the price indicated in our ad and report any errors to store personnel. If errors are not corrected to your satisfaction, please advise the store manager.

IV. Respondent shall not be subject to any of the provisions of this order to the extent that such provisions shall have been rendered inconsistent with the Trade Regulation Rule regarding Retail Food Store Advertising and Marketing Practices, 16 C.F.R. 424 (1977) because of any future amendment to that rule.

V. *It is further ordered,* That:

A. Respondent shall forthwith deliver a copy of this order to each of its officers (excluding assistant officers) and to other of its personnel in its Retail Divisions (down to the level of and including store managers) who, directly or indirectly, have any responsibilities relating to pricemarking and charging out of advertised items in respondent's retail food stores, and respondent shall secure a signed statement acknowledging receipt of said order from each such person.

B. Respondent shall maintain a surveillance program adequate to reveal whether the business practices of its retail food stores conform to this order and shall upon request inform the duly authorized representative of the Commission as to the nature of such program.

C. Respondent shall, for a period of three years subsequent to the date of this order:

(1) Maintain business records which show the efforts taken to achieve continuing compliance with the terms and provisions of this order; and

(2) Furnish to the Federal Trade Commission copies of the records to be maintained under subparagraph (1) above, upon written request by any of its duly authorized representatives.

D. Respondent shall, all other provisions of this order notwithstanding, within 90 days following the end of each year, for a period of three years from the date this order becomes final, file with the Commission a report setting forth in detail the manner and form in which it has complied with this order in the preceding year.

It is further ordered, That respondent shall notify the Commission at least thirty days prior to any proposed change in the corporate respondent, such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the respondent which may affect compliance obligations arising out of this order.

It is further ordered, That the respondent herein shall within 60 days after service upon it of this order, file with the Commission a report in writing, setting forth in detail the manner and form in which it has complied with this order.

IN THE MATTER OF

USLIFE CREDIT CORPORATION, ET AL.

ORDER, OPINION, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION AND TRUTH IN LENDING ACTS

Docket 9057. Complaint, Sept. 26, 1975—Final Order, May 23, 1978

This order, among other things, requires a Schaumburg, Ill. finance company and its parent corporation to cease, in connection with the extension of consumer credit, failing to provide consumers with the material and disclosures required by Federal Reserve System regulations.

Appearances

For the Commission: *Michael E.K. Mpras* and *Robert L. Patterson.*

For the respondents: *Edward W. Keane* and *Bruce E. Clark, Sullivan & Cromwell.*

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, the Truth in Lending Act and the implementing regulation promulgated thereunder, and by virtue of the authority vested in it by said Acts, the Federal Trade Commission, having reason to believe that USLIFE Credit Corporation, a corporation, and USLIFE Corporation, a corporation, hereinafter sometimes referred to as respondents, have violated the provisions of said Acts and the implementing regulation, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent USLIFE Credit Corporation is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware with its principal office and place of business located at 1300 North Meacham Road, Schaumburg, Illinois. Respondent USLIFE Credit Corporation is a wholly-owned subsidiary of USLIFE Corporation.

Respondent USLIFE Corporation is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York with its principal office and place of business located at 125 Maiden Lane, New York, New York.

Respondent USLIFE Credit Corporation operates through approximately two-hundred thirteen (213) wholly-owned subsidiary loan offices located in twenty (20) States of the United States. Each subsidiary is incorporated in the respective state in which it is located under such names as USLIFE Credit Corporation, Quality Finance

Corporation, State Securities, Inc., Sterling Finance Company, Clermont Finance Company, Courtesy Finance Company, North American Finance Company, Best Finance Company and Midland Finance Company. [2]

Respondents USLIFE Corporation and USLIFE Credit Corporation formulate and control the policies, acts and practices of each of the wholly-owned subsidiaries, including the acts and practices hereinafter set forth.

The aforementioned respondents and their subsidiaries cooperate and act together in carrying out the acts and practices hereinafter set forth.

PAR. 2. Respondents by and through their corporate subsidiary structure are now, and for some time last past have been, engaged in the offering to extend, and the extension of, consumer credit to the public.

PAR. 3. In the ordinary course and conduct of their business, as aforesaid, respondents regularly extend consumer credit, as "consumer credit" is defined in Regulation Z, the implementing regulation of the Truth in Lending Act, duly promulgated by the Board of Governors of the Federal Reserve System.

PAR. 4. Subsequent to July 1, 1969, respondents, in the ordinary course and conduct of their business as aforesaid, have charged, and are now charging, for credit life and/or credit accident and health (disability) insurance a substantial number of consumers who obtained a consumer loan from respondents.

Typical and illustrative, but not all-inclusive of the circumstances in which such insurance charges are incurred by consumers, are the following:

1. During the consumer's contact with respondents, respondents' personnel orally quote a monthly repayment figure which includes charges for credit life and/or credit accident and health (disability) insurance.

2. Respondents' personnel automatically include charges for credit life and/or credit accident and health (disability) insurance on the Loan Agreement, and, unless the consumer specifically objects to the inclusion of the charges for such insurance, the coverage becomes part of the credit transaction.

3. On that portion of the Loan Agreement which contains the statements "I desire credit life insurance," or "I desire credit life insurance and disability insurance," respondents' personnel, without the permission or authority of the consumer, place an "x" on the line for the borrower's signature. [3]

4. The Loan Agreement, filled out as indicated above, is presented

to the consumer for two signatures. The consumer is not told of the purpose of each signature. These signatures are intended (1) to indicate the consumer's desire for the insurance coverage, and (2) to acknowledge the consumer's receipt of the executed Loan Agreement.

5. Respondents' personnel place the charges for credit life and/or credit accident and health (disability) insurance in the "Record of Disbursements" section of the Loan Agreement, and these charges become part of the "amount financed," but are not included in the finance charge and thus the annual percentage rate is improperly computed.

PAR. 5. By and through the acts and practices described in Paragraph Four, and others of similar import, meaning and consequence, but not specifically set forth herein, respondents, in a substantial number of instances, obtain consumers' signatures through practices which operate, directly or indirectly, to defeat the elective language of the insurance authorization disclosures by obscuring from consumers knowledge about the option, by misrepresenting to consumers that their signatures are necessary solely for the purpose of consummating the credit transaction, and by discouraging the declination of the coverage when it is questioned. These practices have the effect of preventing substantial numbers of consumers from exercising their own independent, voluntary choice whether to obtain credit life and/or credit accident and health (disability) insurance.

Therefore, respondents, in a substantial number of instances, induce their customers to incur charges for credit life and credit accident and health (disability) insurance without said customers making a knowing, affirmative election to have such insurance and, thereby, respondents have failed to obtain from each of their customers a "specific dated and separately signed affirmative written indication of [their] desire" to obtain such insurance, as required by Section 226.4(a)(5) of Regulation Z, in spite of the existence of language to the contrary in the loan disclosure statement.

PAR. 6. By and through the acts and practices described in Paragraphs Four and Five hereof, respondents have failed to include the charges for credit life and/or credit accident and health (disability) insurance in the finance charge when a specific dated and separately signed affirmative written indication of the consumer's desire for such insurance has not been obtained as required by Section 226.4(a)(5) of Regulation Z, and thereby respondents: **[4]**

1. Failed to compute and disclose accurately the "finance charge," as required by Sections 226.4 and 226.8 of Regulation Z; and
2. Failed to compute and disclose accurately the "annual percent-

age rate" to the nearest quarter of one percent, as required by Sections 226.5 and 226.8 of Regulation Z.

PAR. 7. In the further course and conduct of their business as aforesaid, respondents obtain borrowers' signature on that portion of the Loan Agreement which contains the statements "I desire credit life insurance," or "I desire credit life insurance and disability insurance," and said signatures are not specifically dated as required by Section 226.4(a)(5) of Regulation Z.

PAR. 8. Pursuant to Section 103(q) of the Truth in Lending Act, respondents' aforesaid failure to comply with Sections 226.4, 226.5 and 226.8 of Regulation Z constitute violations of that Act and, pursuant to Section 108 thereof, respondents have thereby violated the Federal Trade Commission Act.

INITIAL DECISION BY JOSEPH P. DUFRESNE, ADMINISTRATIVE LAW JUDGE

JANUARY 27, 1977

PRELIMINARY STATEMENT

In a complaint dated September 26, 1975, the Federal Trade Commission (Commission) charged respondents, USLIFE Credit Corporation (USLIFE Credit) and its parent, USLIFE Corporation (USLIFE), with violations of the Federal Trade Commission Act (15 U.S.C. 41, *et seq.*), the Truth in Lending Act (15 U.S.C. 1601, *et seq.*) and its implementing regulation (Regulation Z - 12 C.F.R. 226) (Complaint, ¶¶ One and Eight). The gravamen of the charges is that in offering to extend and in extending consumer credit to the public: [2]

(1) Prospective borrowers were orally quoted a monthly repayment figure which included charges for credit life and/or credit accident and health (disability) insurance (Complaint, ¶ Four, 1);

(2) Charges for credit life and/or credit accident and health (disability) insurance were automatically included in loan agreements unless the borrower specifically objected to their inclusion (Complaint, ¶ Four, 2);

(3) X's were placed on loan agreements on the lines calling for the borrower's signature to indicate he or she wished to have credit life and/or disability insurance without the borrower's permission or authority (Complaint, ¶ Four, 3);

(4) When loan agreements, filled out as indicated above, were presented to the borrower, he was not told the purpose of the two signatures called for (*i.e.*, one to indicate insurance was desired and the

other to acknowledge receipt of the executed loan agreement) (Complaint, ¶ Four, 4); and

(5) Premium costs of insurance were included in the "Record of Disbursement" section of the loan agreement thus becoming part of the amount financed, but such premiums were not included in the finance charge and therefore the "Annual Percentage Rate" was improperly computed (Complaint, ¶ Four, 5).

The alleged result of these and similar acts and practices was that the language on the loan agreement that insurance was optional was defeated:

> . . . by obscuring from consumers [borrowers] knowledge about the option, by misrepresenting to consumers that their signatures are necessary solely for the purpose of consummating the credit transaction, and by discouraging the declination of the coverage when it is questioned.

[3] It was further alleged that as a consequence:

> . . . respondents, in a substantial number of instances, induce their customers to incur charges for credit life and credit accident and health (disability) insurance without said customer making a knowing, affirmative election to have such insurance and, thereby, respondents have failed to obtain from each of their customers "a specific dated and separately signed affirmative written indication of [their] desire" to obtain such insurance, as required by Section 226.4(a)(5) of Regulation Z, in spite of the existence of language to the contrary in the loan disclosure statement. (Complaint, ¶ Five)

In addition, respondents were charged with having failed to compute and disclose accurately: (1) the finance charge as required by Sections 226.4 and 226.8 of Regulation Z; and (2) the annual percentage rate to the nearest quarter of one percent, as required by Sections 226.5 and 226.8 of Regulation Z. These violations allegedly occurred because respondents did not ". . . include the charges for credit life and/or credit accident and health (disability) insurance in the finance charge when a specific dated and separately signed affirmative written indication of the consumer's desire for such insurance has not been obtained as required by Section 226.4(a)(5) of Regulation Z . . . ." (Complaint, ¶ Six)

Respondents also were charged with violating Section 226.4(a)(5) of Regulation Z because borrowers' signatures in the "insurance" section of the loan agreement ". . . [were] not specifically dated . . . ." (Complaint, ¶ Seven)

In their answer, respondents asserted the following defenses:

(1) The complaint, as a matter of law, did not charge either respondent with a violation of the Truth in Lending Act, the Federal Trade Commission Act, any other act within the jurisdiction of the

Commission, or any valid rule or regulation promulgated by or to be enforced by the Commission (Answer, FIRST DEFENSE, p. 1); [4]

(2) USLIFE is a holding company not engaged in the business of extending consumer credit to the public and does not formulate or control the policies, acts or practices of USLIFE Credit or any of its subsidiaries or branch offices regarding the manner in which credit life or disability insurance is sold. Participation in and knowledge by USLIFE of the policies, acts and practices of USLIFE Credit, as alleged in the complaint, were disclaimed. Consequently, it was contended that, as a matter of law, USLIFE could not be liable even if the charges in the complaint were proven as to USLIFE Credit and found to be violative of any law, valid rule or regulation (Answer, SECOND DEFENSE, p. 2).

As to the first defense, the "Memorandum And Order Respecting Respondents' Motion For Summary Decision," dated February 9, 1976, denying the motion, which was issued by Administrative Law Judge (ALJ) Needelman, to whom the case originally was assigned, details the refutation of the first defense. Suffice it to say here that a violation of the Truth in Lending and Federal Trade Commission Acts is alleged when a respondent is charged with acts and practices which negate written disclosures called for by the Truth in Lending Act. (See pp. 4–7 of ALJ Needelman's "Memorandum and Order . . ." and discussion *infra* under "Did Customers Know That Insurance Was Optional?" and "Reliance On A Truth In Lending Theory Vis-A-Vis Proving A Violation Of The FTC Act"). The second defense raised by respondents is discussed below under "Naming USLIFE As A Respondent."

Prehearing conferences were held by ALJ Needelman on January 5, 1976, and by the undersigned on September 8, 1976. On May 18, 1976, the Commission rejected a consent order profferred by respondents, but opposed by complaint counsel. Oral motions for summary decision and to dismiss as to USLIFE were made at the conclusion of the presentation of the case-in-chief (Tr. 832–37, 839). These were denied (Tr. 842).

The adjudicative hearings were held in Washington, D.C., on September 13–16, 1976, and in Atlanta, Georgia, on September 20–22, 1977. The official record consists of 917 pages of transcript, which includes 132 pages reporting the two prehearing conferences. There are approximately 725 exhibits. [5]

The Striking of Seven Witnesses' Testimony

At the final prehearing conference (PHC) on September 8, 1976, counsel for respondents renewed his earlier request (PHC Tr. 60, 85) that he be furnished in advance of trial with Jencks Act (18 U.S.C. 3500) statements of witnesses which complaint counsel planned to call to testify in connection with his presentation of evidence as a part of the case-in-chief (PHC Tr. 119). Complaint counsel was ordered to hand over any Jencks-type statements by September 10, 1976 (PHC Tr. 123–24). Production on September 10th rather than at the conclusion of the direct examination of the witnesses was ordered since this approach would more fully apprise counsel for respondents of witnesses' expected testimony, and would make cross-examination possible without either a recess or requiring counsel for respondents to speed-read the statements of the witnesses or otherwise necessitating delay in defense counsel completing his questioning of complaint counsel's witnesses while such statements were reviewed.

Although *Inter-State Builders, Inc.*, 69 F.T.C. 1152, 1165–67 (1966), and *Basic Books, Inc.* v. *F.T.C.*, 276 F.2d 718, 722 (7th Cir. 1960) hold that Jencks statements may not be demanded and need not be produced until the end of a witness' direct testimony, these decisions were made prior to the Commission's 1967 amendment of its rules providing for detailed discovery procedures. See 3 CCH Trade Reg. Rep. ¶9625, at 17,195. My order is in harmony with the Commission's position in more recent years favoring maximum pretrial discovery, without prejudice to either side, in order to expedite hearings.

In accordance with the order, complaint counsel stated, prior to the start of the adjudicative hearings, that he had provided counsel for respondents with "all the Jencks Act materials which constituted interview reports that we conducted . . ." (Tr. 5). However, in the course of questioning complaint counsel's first "borrower" witness, Ms. Lillian B. Brooks (Tr. 267–302), it was disclosed that the consumer protection specialist who had interviewed her during the investigation had made substantially verbatim notes of what Ms. Brooks said but that such notes had not been turned over to respondents' counsel (Tr. 290). Ms. Brooks testified that she read the notes as they were being made by the investigator and was asked if what had been written was correct (Tr. 293). [6] She also said that she was asked if she would and that she did sign them (Tr. 289, 293–94). On the following day, the investigator testified that, in accordance with the investigator's customary practice, the notes taken were disposed of after a report of the interview was prepared (Tr. 389, 403). Testimony by the investigator to the effect that the witness did not sign the notes (Tr. 387–88, 390) was not persuasive. Following a request by counsel for respondents, I ordered that the testimony of Ms. Brooks be stricken (Tr. 297–301, 409).

It is worthy of specific mention that complaint counsel clearly was unaware before Ms. Brooks testified that any signed statement was obtained (Tr. 291) or that any such statement had been disposed of (Tr. 291, 294–95). It also is clear that he made extensive efforts to locate the notes once he learned about them (Tr. 299, 379–80).

Because interview notes qualifying as Jencks-type statements relating to the testimony of Mr. William M. Curtin (Tr. 346–79), the third witness called by complaint counsel, were not produced, his testimony also was stricken (Tr. 379). Although Mr. Curtin testified that he did not sign the notes (Tr. 348), he said that he reviewed them and verified that what had been written by the investigator was accurate (Tr. 348, 355). In addition to the testimony of these two, the testimony of five other "borrower" witnesses—Stafford DeLoatch (Tr. 426–61), Mary Louise Knieser (Tr. 463–92), Robert Edward Garner (Tr. 493–518), Eziekiel Moore (Tr. 519–52), and Milton Dickerson (Tr. 792–829)—was stricken (Tr. 461, 492, 518, 553, 803) because the information elicited led me to conclude that Jencks statements had been obtained which complaint counsel was unable to furnish to counsel for respondents.

The Requirements of The Jencks Act

The Jencks Act, in pertinent part, calls for the government, after demand by defendants, to hand over, at the conclusion of the direct examination, statements and reports "in the possession of the United States" of witnesses it calls to testify against a defendant (18 U.S.C. 3500(a)) ". . . which relates to the subject matter as to which the witness has testified" (§ 3500(b)). Also see S. Rep. No. 981, 85th Cong., 1st Sess. 3 (1957). Section 3500(d) of the Act provides that if the government "elects not to comply . . ." the testimony is to be stricken or a "mistrial [is to] be declared." A Commission opinion to the effect that striking the testimony is appropriate in an administrative proceeding in such circumstance is *R. H. Macy & Co.*, 69 F.T.C. 1108 at 1109 (1966). [7]

Section 3500(e) of the Act provides that a "statement" is (1) a document which is written and signed or otherwise adopted or approved by the interviewee/witness, or; (2) "a stenographic, mechanical, electrical or other recording, or a transcription thereof, which is a substantially verbatim recital of an oral statement" made by the interviewee/witness and "recorded contemporaneously with the making of such oral statement."

It is well established that Jencks Act procedures apply to administrative proceedings and that it is for the administrative law judge to determine whether a witness' own words were recorded or whether only a summarization of the witness' remarks was made. See *Inter-*

State, supra, 69 F.T.C. 1157–65, 1171. Also see *Ernest Mark High,* 56 F.T.C. 625, 633 (1959).

Since the witnesses' own words were recorded in the notes made by the investigator, those notes qualified as Jencks-type statements to which counsel for respondents was entitled on the basis of the decision of the Supreme Court in *Goldberg* v. *United States,* 44 U.S.L.W. 4424 (1976). In that decision the Supreme Court said that a Jencks statement is created when government investigators or trial lawyers (1) question the witness during an interview about what he ". . . just said to make sure that they got it down correctly," (2) "occasionally read back to see whether or not they correctly understood . . .," or (3) have the witness correct the notes (44 U.S.L.W. at 4426). Also see *Palermo* v. *United States,* 360 U.S. 343, 352–53 (1959); *Campbell* v. *United States,* 373 U.S. 487, 492–97 (1963).

There is language in a number of decisions in criminal cases to the effect that innocent, good faith destruction of an investigator's/attorney's notes not within the ambit of the Jencks Act in the course of routine administrative procedure is not the equivalent of noncompliance with an order to produce. See *United States* v. *Aviles,* 197 F. Supp. 536, 556 (S.D.N.Y. 1961), *aff'd,* 315 F.2d 186 (2d Cir. 1963), *remanded sub nomine, Evola* v. *United States,* 375 U.S. 32 (1963), *aff'd on remand,* 337 F.2d 552 (1964), *cert. denied,* 380 U.S. 906 (1965); also see 18 U.S.C.A. 3500 Part 2, Ch. 223, n.98. Cases having to do with destruction of notes which are within the ambit of the Jencks Act normally point out that the information in the notes was available in the reports provided to counsel for the defendant (*e.g., United States* v. *Covello,* 410 F.2d 536, 545 (2d Cir. 1969), *cert. denied,* 396 U.S. 879 (1969), *rehearing denied,* 397 U.S. 929 (1970)). How one could be certain that the reports, in fact, contained *all* notes qualifying as Jencks Act statements is not clear. [8] Due process considerations require that counsel for defendants/respondents should be provided with such statements and be given the opportunity to judge whether information they contain as to what the witness said prior to testifying, as reflected in the Jencks notes/statements, comports with what the witness says while testifying.

With regard to the innocent disposition of such notes, as happened here, in *United States* v. *Bryant,* 439 F.2d 642, 652 (D.C. Cir. 1971), the court said that sanctions for nondisclosure of Jencks statements based on loss of evidence will be invoked ". . . unless the Government can show that it has promulgated, enforced and attempted in good faith to follow rigorous and systematic procedures designed to preserve *all* discoverable evidence gathered in the course of a criminal investigation. The burden, of course, is on the Government to make this showing." Also see *United States* v. *Perry*, 471 F.2d 1057, 1062–64 (D.C. Cir. 1972) and *United States* v. *Ferguson*, 498 F.2d 1001 n.3 at 1011 (D.C. Cir. 1974). No showing that either oral or written instructions were provided to the investigator or included in standard operating procedure manuals which detailed the handling of Jencks Act statements was offered at the hearing. Consequently, the sanction of striking the testimony of these seven borrower witnesses has been maintained.

Prior to closing the record the following question was certified to the Commission:

> Should the testimony of witnesses be stricken after the administrative law judge concludes that a Jencks statement was obtained and complaint counsel cannot comply with the order to provide it to counsel for respondents, even though complaint counsel was unaware that what constituted a Jencks statement had been obtained during the investigation and that it had been innocently destroyed? (Order dated October 8, 1976.)

The certification was rejected as not presenting the type of controlling question of law or policy which merits interlocutory consideration under Section 3.23(b) of the Commission's Rules of Practice; however the "Order Rejecting Certification" dated November 2, 1976, reflects that the matter might be considered on appeal. [9]

The testimony which was stricken remains a part of the record because the procedure followed at trial was to permit *voir dire* of each borrower witness by counsel for respondents, have the direct and cross-examination conducted, and then rule as to whether the testimony should be stricken. This testimony, however, has not been considered in connection with the preparation of the initial decision.

Complaint counsel's request to call six additional witnesses, which is mentioned in the "Order Re Briefing Schedule" dated November 12, 1976, was denied because complaint counsel advised that the ground to be covered would be substantially the same as that already in the record which had not been stricken and the undersigned was of the view that hearing the additional witnesses would serve no useful purpose. In that same order the record was closed and dates were set for submittal of proposed findings and orders with reasons therefor by December 10, 1976, and for any replies thereto by December 23, 1976.

Bases for the Findings of Fact; Abbreviations Used

The findings of fact following are based on a review of the allegations made in the complaint, respondents' answer, the documentary evidence, and consideration of the demeanor of the witnesses, including an eidetic recollection of several of them. In addition, the proposed findings of fact, conclusions and proposed orders, together with reasons and briefs in support thereof filed by both sides have been given careful consideration. To the extent not adopted by this decision in the form proposed or in substance, they are rejected as not supported by the record or as immaterial.

For the convenience of the Commission and other readers of this initial decision, the findings of fact include references to supporting evidentiary items in the record. Such references are intended to serve as guides to the testimony, evidence and exhibits supporting the findings of fact. They do not necessarily represent complete summaries of the evidence considered in arriving at such findings. The following abbreviations have been used: **[10]**

Tr. – Transcript, preceded by the name of the witness and followed by the page number.

CX – Commission's Exhibit, followed by number of exhibit being referenced.

RX – Respondents' Exhibit, followed by number of exhibit being referenced.

CCPF – Complaint Counsel's Proposed Findings.

RPF – Respondents' Proposed Findings.

FINDINGS OF FACT

The Respondents

1. USLIFE was organized, exists and does business under and by virtue of the laws of the State of New York. Its principal office and place of business is located at 125 Maiden Lane, New York, New York (Admitted, Answer, ¶ 1(a), p. 2).

2. USLIFE Credit was organized, exists and does business under and by virtue of the laws of the State of Delaware (Admitted, Answer, ¶ 1(a), p. 2). It is engaged in the business of regularly extending consumer credit to the public directly or through its subsidiaries (Admitted, Answer, ¶ 2, p. 4 and ¶ 3, p. 5) and is in competition with nationally known finance companies such as Household Finance and Beneficial Finance Associates (Beckley, Tr. 145). The firm's principal office and place of business is located at 1300 North Meacham Road, Schaumberg, Illinois. USLIFE Credit is a wholly-owned subsidiary of USLIFE (Admitted, Answer, ¶ 1(a), p. 2).

3. USLIFE Credit, directly or though subsidiaries, operates approximately 220 branch offices in 20 states (Admitted, Answer, ¶ 1(b), p.3). Not all branch offices are operated under the name USLIFE Credit (Admitted, Answer, ¶ 1(b), p. 3). As of April 1, 1974, other names used were: Quality Finance Company, Midland Finance Company, State Securities, Inc., Sterling Finance Company, Best Finance

Company, North American Finance Company, Clermont Finance Company, Courtesy Finance Company, and USLIFE Credit Industrial (CX 5). The states in which operations were conducted as of April 1974 were Alabama, Arizona, Florida, Georgia, Illinois, Kentucky, Louisiana, Maryland, Michigan, Missouri, Nevada, New Mexico, North Carolina, Ohio, Oklahoma, Pennsylvania, South Carolina, Tennessee, Texas, and West Virginia (CS 5). [11]

4. USLIFE Credit formulates and controls the policies, acts and practices of its subsidiaries and branch offices regarding the manner in which credit life and disability insurance is sold (Answer, ¶ 1(c), p. 3).

5. USLIFE has knowledge of the loan forms used by USLIFE Credit and could order discontinuance of the use of such forms (Giuliano, Tr. 203–04; First CCPF). USLIFE exercises approval authority over the annual budget of USLIFE Credit (Beckley, Tr. 62; Dunn, Tr. 175–76). USLIFE also must give its approval before USLIFE Credit may buy other companies and is notified when USLIFE Credit decides that a branch office is to be closed (Beckley, Tr. 59–61; Dunn, Tr. 177). USLIFE has the authority and power to overrule the decision to close a branch office (Dunn, Tr. 177).

6. USLIFE Credit has 16 officers and 5 directors. Two of the directors are officers of USLIFE. No officer of USLIFE Credit is an officer or director of USLIFE (RPF 6).

7. USLIFE has 27 officers and 15 directors. One officer/director of USLIFE is a director of USLIFE Credit and another director serves on both boards. No director/officer of USLIFE is also an officer of USLIFE Credit (RPF 5).

8. Mr. Gordon H. Crosby, JR., is the Chairman of the Board of both USLIFE and USLIFE Credit (RX 30a–b). The USLIFE Executive Vice-President of Financial Services, Mr. Samuel Giuliano, who is the liaison officer between respondents, also is a director of USLIFE Credit. Periodically he meets with the Chairman of the Board and chief executive officers to review the financial posture of USLIFE Credit in the light of predetermined, jointly-agreed-upon objectives of the credit company (Giuliano, Tr. 197–201).

9. The following table prepared from information in USLIFE's 1975 annual report indicates the level of its operations:

	1975 (000)	1974 (000)
Net Income	$49,317	$46,074
Total Assets	1,950,901	1,837,249
Total Liabilities	1,622,327	1,537,151

Life Insurance in Force	17,881,058	17,013,034
Consumer Credit Receivables	155,209	143,337

(RX 21, pp. 1 and 19.)

[12] *Sale Of Insurance*

10. The policy of USLIFE Credit has always been that credit life and credit disability insurance coverage is optional and that loan approvals are not contingent upon the customer's decision to accept or reject insurance (RPF 19). USLIFE Credit does, however, attempt to sell insurance to borrowers (Dunn, Tr. 181–83; Miles Tr. 862; RPF 46). When sales resistance was encountered, employees sometimes would say: "Well, the company's policy was we like to have insurance on every loan . . . that the insurance was a good thing for them . . . but there was nothing said to the customer if they didn't take the insurance they couldn't get the loan." (George, Tr. 252.) If successful in selling the insurance, the firm arranges for credit life and/or accident and health (disability) coverage (Admitted, Answer, ¶ 4(b), pp. 5–6). Eighty to ninety percent of USLIFE Credit borrowers purchased insurance to cover the amounts of their loans (Miles, Tr. 855).

11. The loan application form, which is filled in by employees of USLIFE Credit using information provided by prospective borrowers (Beckley, Tr. 116–17; Stricklen, Tr. 221–22; George, Tr. 247), does not have a space for entry of information as to whether insurance is or is not desired. It does have spaces for information as to the amounts of insurance premium refunds a borrower with a previous loan will have in taking out the new loan and for the premiums on insurance to cover the new loan (RX 7).

12. The loan agreement forms used disclose that the purchase of insurance to cover loans is optional (CXs 95, 98, 103, 106, 110, 116, 119–20, 122, 125, 135–414). Witnesses who are officers of the firms testified that insurance was and is optional and written instructions to the branch offices were to the same effect (Beckley, Tr. 84–87, 89, 94, 130–31, 143; Dunn, Tr. 185; RXs 2, 3).

13. In the body of the loan agreement forms there is a section which the borrower is to date and sign to indicate whether he (1) does not want insurance, (2) wants credit life insurance, or (3) wants both credit life and disability insurance (CXs 95, 98, 103, 106, 110, 116, 119–20, 122, 125, 135–414). [13] Usually this section bears a caption such as "Optional Insurance Notice" or "Insurance Notice" (*e.g.*, CXs 95, 106, 116); however, some sections have no such caption (*e.g.*, CXs 148, 150). There was testimony and some exhibits show that the borrower does

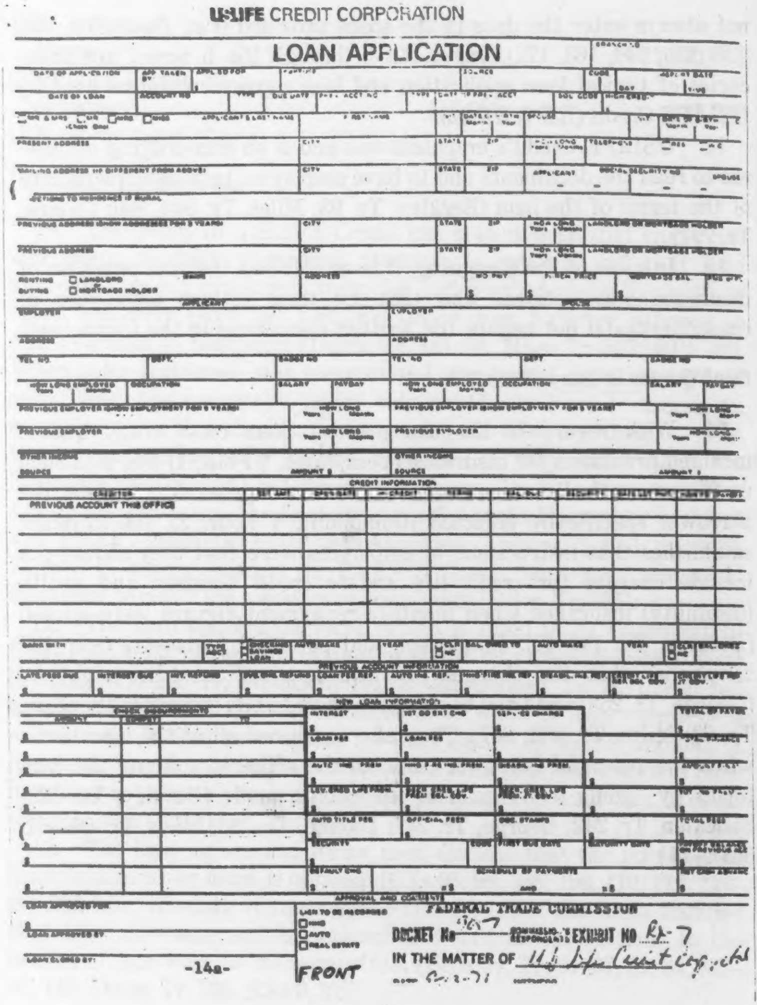
not always enter the date in the space provided (*e.g.*, *Dunn*, Tr. 186, CXs 135, 140, 163, 172). Pages 14a–b through 15a–h hereof are photo copies of typical loan application and loan agreement forms used by USLIFE Credit (RX 7, RX 32).

14. USLIFE Credit's emphasis was and is on encouraging borrowers to read the documents and to have employees provide explanations of the terms of the loan (Beckley, Tr. 93; Miles, Tr. 845, 860; Dionne, Tr. 791).

15. In view of the foregoing, it is established that the purchase of insurance was optional and that by their actions employees of respondents did not negate the written disclosures in the forms used.

Oral Quotes of Loan Costs

16. With regard to the charges that loan costs orally quoted included premiums for insurance (Complaint, ¶ Four, 1) and that such costs automatically were included in loan agreements unless the borrower specifically objected (Complaint, ¶ Four, 2), the evidence establishes that instructions to employees were that they should not include charges for credit life and/or credit accident and health (disability) insurance when monthly repayment figures were quoted (Beckley, Tr. 140–41). Employees told potential borrowers over the telephone what the charges for insurance on the loan might be (George, Tr. 253) and tried to persuade them to buy insurance (Beckley, Tr. 93; Miles, Tr. 862, 867). They also explained all of the loan terms when the potential borrower came to the office to execute the loan forms by "going over" each of the entries made (Beckley, Tr. 129; Stricklen, Tr. 242; George, Tr. 247; Dionne, Tr. 791, Miles, Tr. 860–61, 865). [14]



USLIFE CREDIT CORPORATION

LOAN APPLICATION

DATE OF APPLICATION

DATE OF LOAN

ACCOUNT NO

PRESENT ADDRESS

CITY

STATE

ZIP

TELEPHONE

APPLICANT

SPOUSE

PREVIOUS ADDRESS

RENTING ☐ LANDLORD

BUYING ☐ MORTGAGE HOLDER

EMPLOYER

ADDRESS

TEL NO.

DEPT.

OCCUPATION

SALARY

PAYDAY

PREVIOUS EMPLOYER

OTHER INCOME

SOURCE

AMOUNT $

CREDIT INFORMATION

PREVIOUS ACCOUNT THIS OFFICE

PREVIOUS ACCOUNT INFORMATION

NEW LOAN INFORMATION

INTEREST

LOAN FEE

AUTO TITLE FEE

SECURITY

SCHEDULE OF PAYMENTS

APPROVAL AND COMMENTS

☐

☐ AUTO

☐ REAL ESTATE

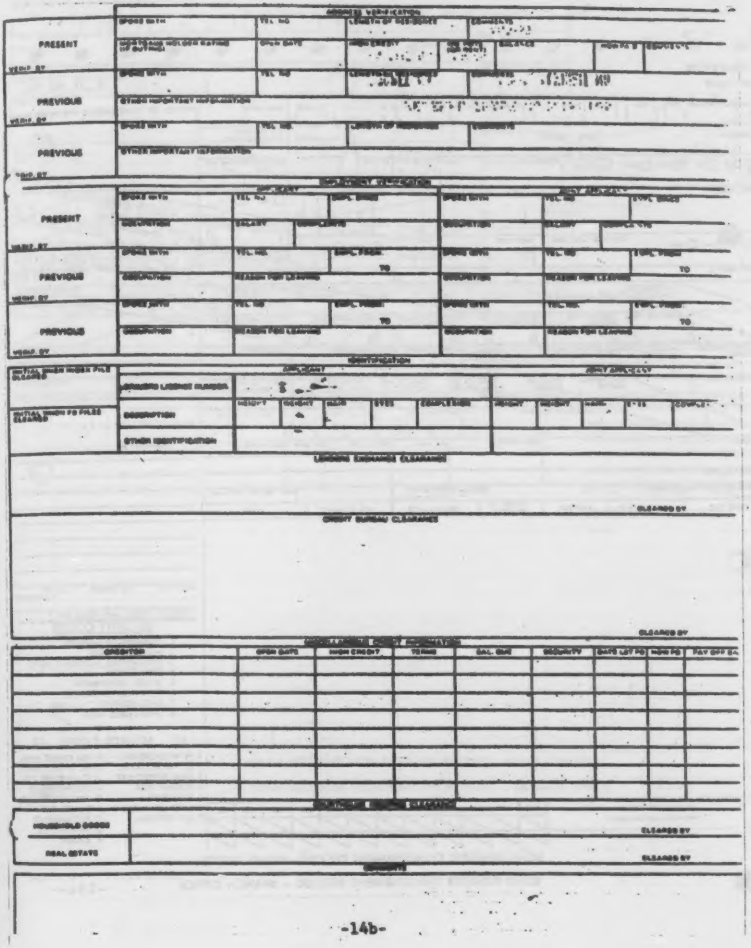
-14a-

FRONT

FEDERAL TRADE COMMISSION

DOCKET No [illegible] COMMISSION'S / RESPONDENT'S EXHIBIT NO Rx-7

IN THE MATTER OF U.S. Life Credit Corporation



ADDRESS VERIFICATION

PRESENT

PREVIOUS

PREVIOUS

EMPLOYMENT VERIFICATION

APPLICANT

JOINT APPLICANT

PRESENT

PREVIOUS

TO

PREVIOUS

TO

IDENTIFICATION

DESCRIPTION

OTHER IDENTIFICATION

LENDERS EXCHANGE CLEARANCE

CLEARED BY

CREDIT BUREAU CLEARANCE

CLEARED BY

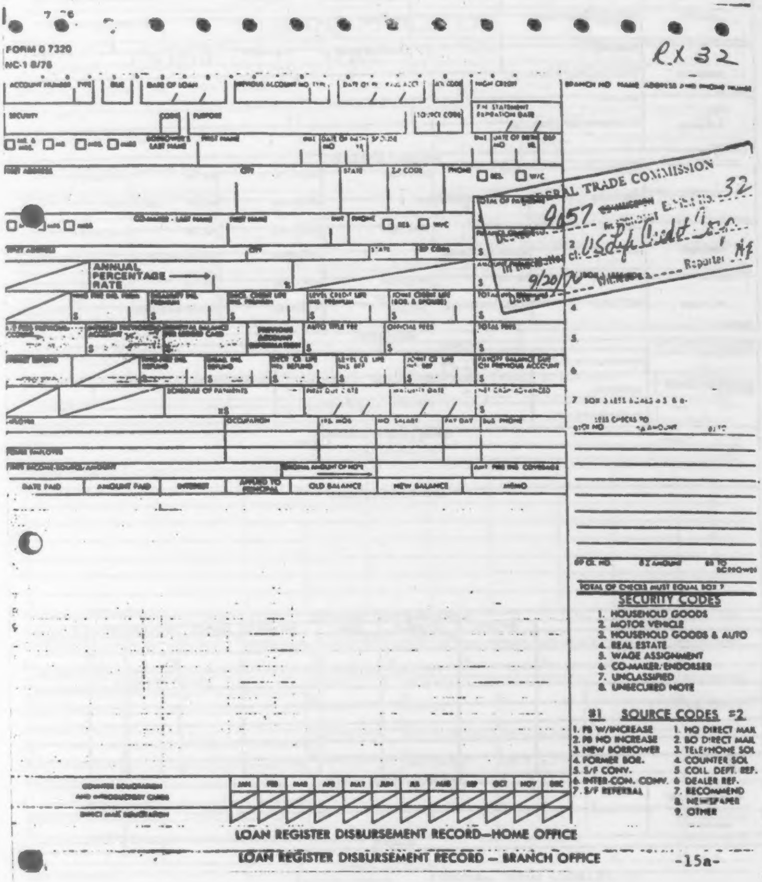
CREDITOR	OPEN DATE	HIGH CREDIT	TERMS	BAL. DUE	SECURITY	DATE LST PD	HOW PD	PAY OFF BA

HOUSEHOLD GOODS — CLEARED BY

REAL ESTATE — CLEARED BY

COMMENTS

-14b-



FORM 0 7320
NC-1 8/76

RX 32

ACCOUNT NUMBER TYPE | DATE OF LOAN | PREVIOUS ACCOUNT NO. TYPE | HIGH CREDIT

SECURITY | CODE | PURPOSE | SOURCE CODE

CITY | STATE | ZIP CODE | PHONE ☐ RES. ☐ W/C

FIRST NAME | PHONE ☐ RES. ☐ W/C

CITY | STATE | ZIP CODE

ANNUAL PERCENTAGE RATE ⟶ %

LEVEL CREDIT LIFE INS. PREMIUM $ | JOINT CREDIT LIFE (BOR. & SPOUSE) $

AUTO TITLE FEE $ | OFFICIAL FEES $ | TOTAL FEES $

PAYOFF BALANCE ON PREVIOUS ACCOUNT $

SCHEDULE OF PAYMENTS | MATURITY DATE | NET CASH ADVANCED $

OCCUPATION | PAY DAY

DATE PAID	AMOUNT PAID	INTEREST	APPLIED TO PRINCIPAL	OLD BALANCE	NEW BALANCE	MEMO

FEDERAL TRADE COMMISSION
Docket No. 9057
Exhibit No. 32
In the Matter of: US Life Credit Corp.
Date 9/20/76
Reporter HF

TOTAL OF CHECKS MUST EQUAL BOX 7

SECURITY CODES

1. HOUSEHOLD GOODS
2. MOTOR VEHICLE
3. HOUSEHOLD GOODS & AUTO
4. REAL ESTATE
5. WAGE ASSIGNMENT
6. CO-MAKER/ENDORSER
7. UNCLASSIFIED
8. UNSECURED NOTE

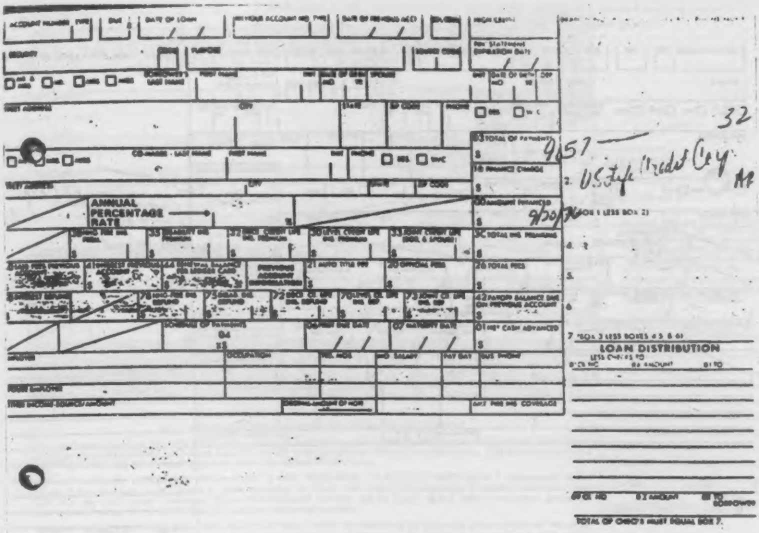
#1	SOURCE CODES #2
1. FB W/INCREASE	1. HO DIRECT MAIL
2. FB NO INCREASE	2. BO DIRECT MAIL
3. NEW BORROWER	3. TELEPHONE SOL.
4. FORMER BOR.	4. COUNTER SOL.
5. S/F CONV.	5. COLL. DEPT. REF.
6. INTER-CON. CONV.	6. DEALER REF.
7. S/F REFERRAL	7. RECOMMEND
	8. NEWSPAPER
	9. OTHER

	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC

LOAN REGISTER DISBURSEMENT RECORD—HOME OFFICE

LOAN REGISTER DISBURSEMENT RECORD — BRANCH OFFICE

-15a-



9,57—

32

2. US Life Credit Corp AP

9/20/7

ANNUAL PERCENTAGE RATE →

%

TOTAL OF PAYMENTS $

FINANCE CHARGE $

AMOUNT FINANCED $

TOTAL INS. PREMIUMS $

TOTAL FEES $

NET CASH ADVANCED $

4.

5.

6

7 BOX 3 LESS BOXES 4 5 & 6

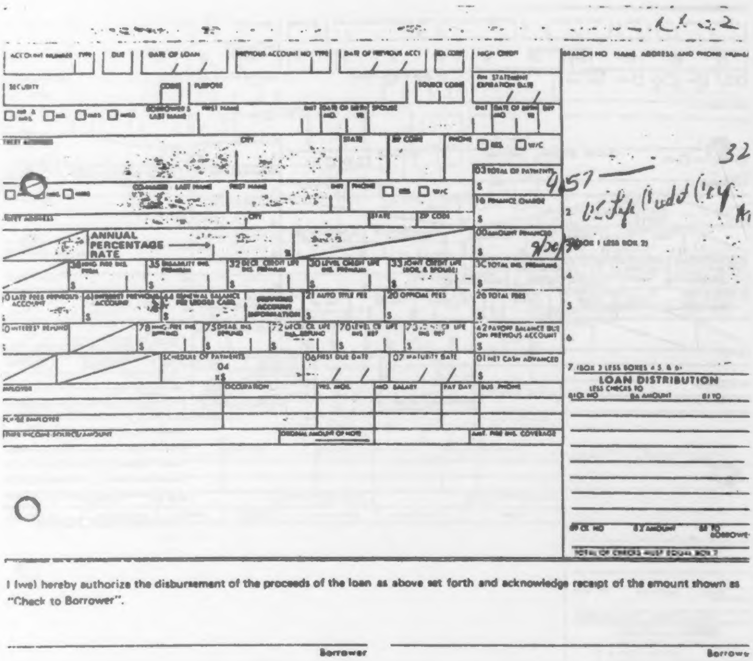
LOAN DISTRIBUTION

LESS CHECKS TO

TOTAL OF CHECKS MUST EQUAL BOX 7.

LOAN REGISTER DISBURSEMENT RECORD—HOME OFFICE

LOAN REGISTER DISBURSEMENT RECORD – BRANCH OFFICE -15b-



ACCOUNT NUMBER TYPE | DUE | DATE OF LOAN | PREVIOUS ACCOUNT NO. TYPE | DATE OF PREVIOUS ACCT | HIGH CREDIT | BRANCH NO. NAME ADDRESS AND PHONE NUMBER

SECURITY | CODE | PURPOSE | SOURCE CODE | STATEMENT EXPIRATION DATE

☐ ☐ ☐ ☐ BORROWER'S LAST NAME | FIRST NAME | DATE OF BIRTH MO. YR. | SPOUSE | DATE OF BIRTH MO. YR.

STREET ADDRESS | CITY | STATE | ZIP CODE | PHONE ☐ RES. ☐ W/C

03 TOTAL OF PAYMENTS $ 4/57 — 32

☐ ☐ ☐ CO-MAKER LAST NAME | FIRST NAME | PHONE ☐ RES. ☐ W/C

10 FINANCE CHARGE $

STREET ADDRESS | CITY | STATE | ZIP CODE

ANNUAL PERCENTAGE RATE → %

00 AMOUNT FINANCED $ (BOX 1 LESS BOX 2)

35 DISABILITY INS. PREMIUM $ | 32 DECR. CREDIT LIFE INS. PREMIUM $ | 30 LEVEL CREDIT LIFE INS. PREMIUM $ | 33 JOINT CREDIT LIFE (BOR. & SPOUSE) $ | 3C TOTAL INS. PREMIUMS $

LATE FEES PREVIOUS ACCOUNT | INTEREST PREVIOUS ACCOUNT $ | 44 RENEWAL BALANCE PER LEDGER CARD $ | PREVIOUS ACCOUNT INFORMATION | 21 AUTO TITLE FEE $ | 20 OFFICIAL FEES $ | 26 TOTAL FEES $

INTEREST REFUND | 78 $ | 75 DISAB. INS. REFUND $ | 72 DECR. CR. LIFE INS. REFUND $ | 70 LEVEL CR. LIFE INS. REF. $ | 73 CR. LIFE INS. REF. $ | 42 PAYOFF BALANCE DUE ON PREVIOUS ACCOUNT $

SCHEDULE OF PAYMENTS 04 X$ | 06 FIRST DUE DATE | 07 MATURITY DATE | 01 NET CASH ADVANCED $

7 (BOX 3 LESS BOXES 4 5 & 6)

EMPLOYER | OCCUPATION | YRS. MOS. | MO. SALARY | PAY DAY | BUS. PHONE

LOAN DISTRIBUTION

LESS CHECKS TO

CK. NO. | AMOUNT | TO

SPOUSE EMPLOYER

OTHER INCOME SOURCE/AMOUNT | ORIGINAL AMOUNT OF NOTE | AMT. INS. COVERAGE

CK. NO. | AMOUNT | TO BORROWER

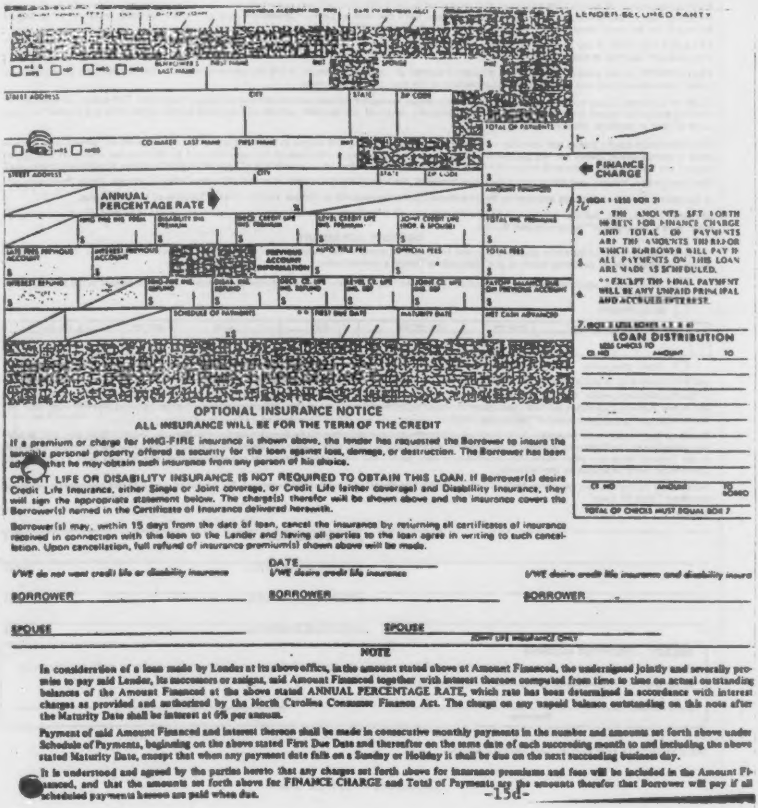
TOTAL OF CHECKS MUST EQUAL BOX 7

I (we) hereby authorize the disbursement of the proceeds of the loan as above set forth and acknowledge receipt of the amount shown as "Check to Borrower".

Borrower

Borrower

LOAN REGISTER DISBURSEMENT RECORD — BRANCH OFFICE -15c-



LENDER-SECURED PARTY

☐ ☐ ☐ ☐ BORROWER'S LAST NAME FIRST NAME INIT. SPOUSE INIT.

STREET ADDRESS CITY STATE ZIP CODE

TOTAL OF PAYMENTS * $

☐ ☐ CO-MAKER LAST NAME FIRST NAME INIT.

STREET ADDRESS CITY STATE ZIP CODE

$ ← FINANCE CHARGE 2

ANNUAL PERCENTAGE RATE ➡ %

AMOUNT FINANCED $

3.

$ $ $ $ $ $

4

5.

$ $ PREVIOUS ACCOUNT INFORMATION $ $ TOTAL FEES $

$ $ $ $ $ $ $

6.

SCHEDULE OF PAYMENTS x$ FIRST DUE DATE MATURITY DATE NET CASH ADVANCED $

* THE AMOUNTS SET FORTH HEREIN FOR FINANCE CHARGE AND TOTAL OF PAYMENTS ARE THE AMOUNTS THEREFOR WHICH BORROWER WILL PAY IF ALL PAYMENTS ON THIS LOAN ARE MADE AS SCHEDULED.

** EXCEPT THE FINAL PAYMENT WILL BE ANY UNPAID PRINCIPAL AND ACCRUED INTEREST.

7.

LOAN DISTRIBUTION

CK NO AMOUNT TO

CK NO AMOUNT TO BORROWER

TOTAL OF CHECKS MUST EQUAL BOX 7

OPTIONAL INSURANCE NOTICE

ALL INSURANCE WILL BE FOR THE TERM OF THE CREDIT

If a premium or charge for HHG-FIRE insurance is shown above, the lender has requested the Borrower to insure the tangible personal property offered as security for the loan against loss, damage, or destruction. The Borrower has been advised that he may obtain such insurance from any person of his choice.

CREDIT LIFE OR DISABILITY INSURANCE IS NOT REQUIRED TO OBTAIN THIS LOAN. If Borrower(s) desire Credit Life Insurance, either Single or Joint coverage, or Credit Life (either coverage) and Disability Insurance, they will sign the appropriate statement below. The charge(s) therefor will be shown above and the insurance covers the Borrower(s) named in the Certificate of Insurance delivered herewith.

Borrower(s) may, within 15 days from the date of loan, cancel the insurance by returning all certificates of insurance received in connection with this loan to the Lender and having all parties to the loan agree in writing to such cancellation. Upon cancellation, full refund of insurance premium(s) shown above will be made.

DATE________________

I/WE do not want credit life or disability insurance *I/WE desire credit life insurance* *I/WE desire credit life insurance and disability insura*

BORROWER____________ BORROWER____________ BORROWER____________

SPOUSE____________ SPOUSE____________
JOINT LIFE INSURANCE ONLY

NOTE

In consideration of a loan made by Lender at its above office, in the amount stated above at Amount Financed, the undersigned jointly and severally promise to pay said Lender, its successors or assigns, said Amount Financed together with interest thereon computed from time to time on actual outstanding balances of the Amount Financed at the above stated ANNUAL PERCENTAGE RATE, which rate has been determined in accordance with interest charges as provided and authorized by the North Carolina Consumer Finance Act. The charge on any unpaid balance outstanding on this note after the Maturity Date shall be interest at 6% per annum.

Payment of said Amount Financed and interest thereon shall be made in consecutive monthly payments in the number and amounts set forth above under Schedule of Payments, beginning on the above stated First Due Date and thereafter on the same date of each succeeding month to and including the above stated Maturity Date, except that when any payment date falls on a Sunday or Holiday it shall be due on the next succeeding business day.

It is understood and agreed by the parties hereto that any charges set forth above for insurance premiums and fees will be included in the Amount Financed, and that the amounts set forth above for FINANCE CHARGE and Total of Payments are the amounts therefor that Borrower will pay if all scheduled payments hereon are paid when due.

-15d-

Every payment received hereon shall be applied first to interest to the actual date payment is received and the remainder thereof to the Amount Financed. Default in making any scheduled or deferred payment hereon when due shall, at Lender's option and without notice or demand, render the entire unpaid balance of the Amount Financed and accrued interest at once due and payable.

DEFAULT CHARGE: If any payment hereon is not made when due, interest will continue to accrue on the unpaid Amount Financed at the above stated rate until such payment is made.

PREPAYMENT: If the unpaid balance of the Amount Financed of this loan is prepaid in full, by whatever means, before the Maturity Date hereof, interest at the above stated rate will be charged thereon only to the date of actual payment.

Cause of action shall arise hereon only with respect to the entire Amount Financed and accrued interest unpaid hereunder. The makers, sureties, endorsers and guarantors hereof severally waive demand for payment, notice of non-payment, protest and notice of protest of this note and consent to extensions of time of payment without notice.

The undersigned hereby jointly and severally authorize the Lender, its agents and assigns to communicate in any manner with any person, firm, corporation or governmental agency for any purpose in connection with the making or collection of the loan evidenced by this note and also waive the right to enforce any claim, action or cause of action which the undersigned may hereafter have for violation of right of privacy by reason of such communications.

The construction, validity, and effect hereof shall be governed by the laws of North Carolina, as modified by the Federal Consumer Credit Protection Act.

A statement of said loan has been delivered to the undersigned Debtor as required by Section 53-181, General Statutes of North Carolina.

SECURITY: If secured, this loan will be secured by a security interest in such of Borrowers' personal property as is described in the below Security Agreement, or in a "Schedule A" listing attached thereto.

SECURITY AGREEMENT

To secure the payment of the above described loan and any future advances to the undersigned, Debtor(s) grant(s) a security interest to the Secured Party in the personal property described below or in a "Schedule A" listing attached hereto.

☐ All furniture, appliances and other household goods and chattels now owned and located in or about Debtor(s) residence at the address shown above.

☐ Motor Vehicle:

YEAR		MAKE	BODY TYPE	MFG./SER. NO.	YEAR		MAKE	BODY TYPE	MFG./SER. NO.
1					2				

☐ Other (describe):

and all accessions to, substitutions for, replacements of and proceeds from the described collateral.

If this Security Agreement includes a motor vehicle, Debtor(s) covenant(s) they will not remove it from the State of their present residence shown above and if this Security Agreement includes other personal property, Debtor(s) covenant(s) they will not remove such other personal property from their residence, without the written consent of the Secured Party.

If default shall occur in the payment of any debt secured hereby or any conditions of this Security Agreement, then the Secured Party may take immediate possession of the Collateral wherever found, with or without legal process, may require the Debtor(s) to assemble the Collateral and make it available to the Secured Party at a place reasonably convenient to both parties and may exercise any rights and remedies granted a Secured Party by the Uniform Commercial Code on default by the Debtor(s).

Borrower(s) hereby execute the above Note and, if applicable, the Security Agreement and acknowledge receipt of a copy of this document executed on the above "Date Of Loan".

Witness

____________________ ____________________ (DEBTOR/BORROWER) SEAL

____________________ ____________________ (DEBTOR/BORROWER) SEAL

____________________ ____________________ (DEBTOR/BORROWER) SEAL

____________________ ____________________ (DEBTOR/BORROWER) SEAL

RECEIPT – PREVIOUS ACCOUNT

Borrower(s) hereby tender payment in full by renewal of the previous account identified above and acknowledge receipt by credit to said account of the unearned finance charge and all insurance premium refunds.

____________________ Borrower ____________________ Borrower

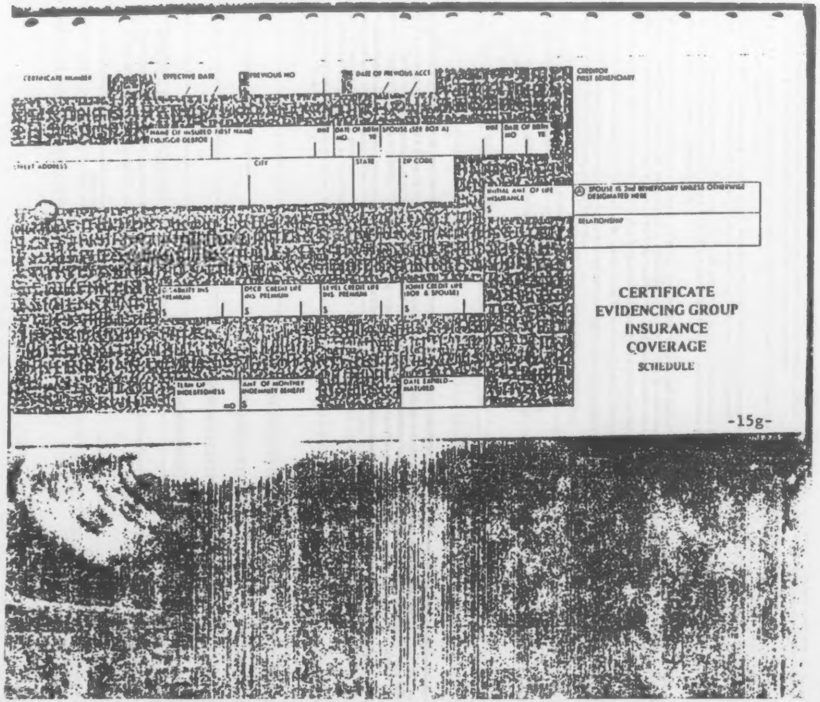
SEE OTHER SIDE FOR IMPORTANT INFORMATION

ORIGINAL — OFFICE COPY

-15e-

Agreed rate of Charge	3% per month on that part of the unpaid principal balance not exceeding $300 and 1½% per month on that part of the unpaid principal balance in excess of $300, but not exceeding $1500, provided however, that after maturity the rate shall be reduced to 6% simple interest per annum on any balance remaining unpaid.

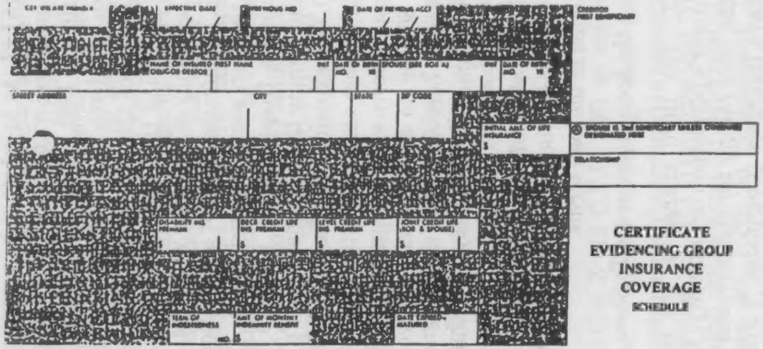
-15f-



CERTIFICATE NUMBER
EFFECTIVE DATE
PREVIOUS NO
DATE OF PREVIOUS ACCT
CREDITOR FIRST BENEFICIARY
NAME OF INSURED FIRST NAME OBLIGOR DEBTOR
AGE
DATE OF BIRTH MO YR
SPOUSE (SEE BOX A)
AGE
DATE OF BIRTH MO YR
STREET ADDRESS
CITY
STATE
ZIP CODE
INITIAL AMT OF LIFE INSURANCE $
Ⓐ SPOUSE IS 2nd BENEFICIARY UNLESS OTHERWISE DESIGNATED HERE
RELATIONSHIP
DISABILITY INS PREMIUM $
DECR CREDIT LIFE INS PREMIUM $
LEVEL CREDIT LIFE INS PREMIUM $
JOINT CREDIT LIFE (DEB & SPOUSE) $
TERM OF INDEBTEDNESS MO
AMT OF MONTHLY INDEMNITY BENEFIT $
DATE EXPIRED—MATURED

CERTIFICATE
EVIDENCING GROUP
INSURANCE
COVERAGE
SCHEDULE

-15g-


EFFECTIVE DATE
PREVIOUS NO
DATE OF PREVIOUS ACCT
CREDITOR FIRST BENEFICIARY
NAME OF INSURED FIRST NAME
DATE OF BIRTH MO. YR
SPOUSE (SEE BOX A)
DATE OF BIRTH MO. YR
STREET ADDRESS
CITY
STATE
ZIP CODE
INITIAL AMT. OF LIFE INSURANCE $
Ⓐ SPOUSE IS 2nd BENEFICIARY UNLESS OTHERWISE DESIGNATED HERE
RELATIONSHIP
DISABILITY INS PREMIUM $
DECR CREDIT LIFE INS PREMIUM $
LEVEL CREDIT LIFE INS PREMIUM $
JOINT CREDIT LIFE (BOR & SPOUSE) $
TERM OF INDEBTEDNESS MO.
AMT OF MONTHLY INDEMNITY BENEFIT $
DATE EXPIRED-MATURED

CERTIFICATE
EVIDENCING GROUP
INSURANCE
COVERAGE
SCHEDULE

-15h-

U-LIFE CREDIT LIFE INSURANCE COMPANY

Schaumburg, Illinois

LIFE CLAIM

1. Policy No. .... __________
2. Initial Amount of Indebtedness .... $__________
3. Amount Paid .... $__________
4. Balance Due .... $__________
5. Number of Monthly Payments in Default at Death .... __________

I hereby certify that the balance due on this account is the amount shown in Line 4.

NOT VALID UNLESS ACCOMPANIED BY CERTIFIED COPY OF DEATH CERTIFICATE.

__________ Date

__________ Creditor

__________ Title

CREDITOR'S MEMORANDUM

[16] 17. As to whether borrowers were apprised that insurance was optional, one witness who had had many loans with USLIFE Credit, his first in 1969, (Eller, Tr. 340) said that he was not informed that he need not have insurance on his loans (Eller, Tr. 334, 338). The testimony of this witness (Tr. 302–45), however, was so contradictory and confusing that little reliance has been placed on it in the face of the testimony of the other witnesses.

18. Insurance was not automatically included when the documents for the loan were prepared (Miles, Tr. 863). The evidence *is* clear that borrowers frequently did not take the time to read the loan papers before signing them (Richardson, Tr. 658, 663–64, 669, 677; Ferrari, Tr. 595). One explained that he was in a hurry (Grant, Tr. 755, 760, 765–66).

19. There also was testimony to the effect that employees did not pressure borrowers to sign any of the loan documents hastily (Miles, Tr. 865) or do anything else by word or act which would hinder or prevent a borrower from taking as much time as he chose to read the loan documents (Richardson, Tr. 658; Grant, Tr. 740, 742; Dionne, Tr. 791).

20. In view of the foregoing, it is established that costs of loans were properly quoted orally and that insurance was not automatically included in the loan terms.

Xs on the Loan Agreements To Show Locations for Signatures

21. The third charge in the complaint was that, without the borrower's permission or authority, Xs were placed on loan agreements on the lines calling for the borrower's signature to indicate he wanted to have insurance (Complaint, ¶ Four, 3). Rather than being used to induce the unwitting purchase of insurance, the evidence established that such marks were placed on the documents as a convenience to facilitate location of the places where the borrowers' signatures were to be affixed (Stricklen, Tr. 239; Richardson, Tr. 649; Grant, Tr. 726–27, 765). In the summer of 1973, employees were instructed to discontinue the practice because of criticism of the use of such check marks expressed at a convention of lenders (Dunn, Tr. 186–87; George, Tr. 256). The fact that employees were instructed to discontinue the practice, however, does not obviate the possibility of violation. See *Montgomery Ward & Co.* v. *F.T.C.*, 379 F.2d 666, 672 (7th Cir. 1967). [17]

22. The evidence is persuasive, in the light of the testimony to the effect that respondents' employees did nothing to pressure, rush, or deceive borrowers into signing anything, that the placing of marks such as Xs on the documents was a convenience rather than a deceptive or pressure tactic.

23. A complementary allegation was that, when loan agreements were presented to borrowers filled out by employees of USLIFE Credit with loan data and the Xs as indicated, the borrowers' signatures required to show that insurance was desired and to acknowledge receipt of the executed loan agreements were not explained (Complaint, ¶ Four, 4). Although the evidence shows that marks were used, it does not establish that it was done for any ulterior purpose or that presentation of the documents marked in this manner for execution by borrowers is a violation of the Truth in Lending Act. The evidence is persuasive that the terms of loans were "gone over" (Findings 14, 16) and that borrowers were given ample opportunity to read the documents (Findings 19, 22).

Computations of the Annual Percentage Rate

24. It was also alleged that since the premium costs of insurance were included in the "Record of Disbursement" section of the loan agreement, such costs became a part of the amount financed but were not included in the finance charge. Hence, the alleged result was that the "Annual Percentage Rate" was improperly computed (Complaint, ¶ Four, 5).

25. Section 226.2(g) of Regulation Z (12 C.F.R. 226) as amended October 28, 1975, provides that the " 'Annual Percentage Rate' means the annual percentage rate of finance charge determined in accordance with § 226.5." In pertinent part, section 226.5(b)(1) provides that "[t]he mathematical equation and technical instructions for determining the annual percentage rate . . . are set forth in Supplement I to Regulation Z which is incorporated in this Part by reference." Reference to Supplement I, however, is unnecessary in connection with this matter because 226.4(a)(5) "Determination of Finance Charge, General Rule" provides that charges for insurance written in connection with a credit transaction are to be included in arriving at the charge *unless:*

> (i) the insurance coverage is not required by the creditor and this fact is clearly and conspicuously disclosed in writing to the customer; and
> (ii) any customer desiring such insurance coverage gives specifically dated and separately signed affirmative written indication of such desire after receiving written disclosure to him of the cost of such insurance.

[18] 26. Since the evidence shows that insurance was and is *not required* (Beckley, Tr. 84), that this fact is clearly and conspicuously disclosed in *writing* to the customer, and that the acts and practices of respondents' employees do not negate the written disclosure, the insurance premiums involved in this case need not be included in the

calculation of the finance charge. The documentary and testimonial evidence shows that customers execute, or always have presented to them for execution, a clearly marked and separately distinguishable section of the loan agreement, which section has to do solely with apprising the customer (1) that he or she need not purchase insurance in order to take out the loan, (2) that he or she may decline to take out insurance, and (3) that he or she has a choice of disability/health or life insurance if any is wanted. (CXs 95, 98, 103, 106, 110, 116, 119–20, 122, 125, 135–414.)

27. The insurance section of loan agreement forms used by respondents also calls for insertion of a date by the customer adjacent to his signature indicating his choice of insurance options (Dunn, Tr. 185–86; CXs 95, 98, 106, 110, 116, 119–20, 122, 125, 135–414) as required by § 226.4(a)(5) in order to exclude insurance premiums from computation of the finance charge. As noted previously, the record indicates that a separate dating by the customer of this section of the loan agreement was not always done (Dunn, Tr. 186). The fact that the date has not been entered in the insurance-is-optional section of otherwise properly dated loan agreement forms, like those in evidence here, has been held to be not violative of § 226.4(a)(5) of Regulation Z. In *In Re Warren*, 387 F. Supp. 1395, 1404 (S.D. Ohio, E.D. 1975) the court explicitly stated:

> Whether the date is at the top of the page on the disclosure statement or separately written next to the credit life request, the purpose of the Truth in Lending Act—to permit the debtor to make an informed credit choice—is equally well-fulfilled.

See also, *Porter* v. *Household Finance Corp. of Columbus*, 385 F. Supp. 336, 345 (S.D. Ohio, E.D. 1974).

[19] 28. I do not agree with the proposal of complaint counsel that a separate piece of paper should be required for insurance disclosures in order for a lender to be in compliance with § 226.4(a)(5) of Regulation Z (Proposed Order, 2(a), (b); CCPF, pp. 38–40). The section merely requires that the election is to be separately signed after premium costs are "disclosed in writing," as they are here (CXs 95, 98, 103, 106, 110, 116, 119–20, 122, 125, 135–414; RXs 12,24), in order to indicate the borrower's choice regarding insurance. Further, complaint counsel acknowledged that the insurance disclosure in respondents' present loan documents is in full compliance with the law (PHC Tr. 13; CCPF, p. 30).

Did Customers Know That Insurance Was Optional?

29. The practices discussed above serve as the basis for the allegations in the complaint to the effect that borrowers are induced to

incur charges for insurance in spite of the insurance-is-optional language and spaces for declining or requesting insurance which are contained in the loan agreement forms (Complaint, ¶ Five). There is no question that conduct which negates written procedures may be shown at trial to prove that, in fact, a requirement existed that insurance had to be purchased. *Fisher* v. *Beneficial Finance Company of Hoxsie*, 383 F. Supp. 895, 900 (D.C.R.I. 1974).

30. Contrary to the suggestion in the complaint that the actions of employees of USLIFE Credit nullified the insurance-is-optional language and that they used deceptive or pressure tactics to place insurance on loans, the evidence shows that borrowers, for the most part, either were aware specifically that insurance was optional or by their actions made it clear that such fact was of little or no interest to them (George, Tr. 253; Findings 15, 18). For example, Ms. Ferrari, signed the optional insurance section (Tr. 581) and testified that she both read and understood it (Tr. 592). Ms. Ferrari also testified that the insurance coverage was discussed but that she was told "If you do not want to take this loan with the insurance, that is one thing; but there is not a place in town that would give you this money without the insurance" (Tr. 572). The suggestion that the employee actions negated the insurance-is-optional language in the form, however, is tempered by the fact that Ms. Ferrari signed the optional insurance section and said that she read and understood it (*supra*). Further, the testimony of Ms. Ferrari makes it obvious that she was hostile toward respondents due to the fact that she felt she had been made to "look ridiculous"—"like a fool"—when she questioned the employee regarding insurance [20] (Tr. 594). Ms. Ferrari said that she did not want to ever see or talk to any USLIFE Credit employee again (Tr. 600) even though she knew later that a refund was being held for her to pick up at the local branch office (Tr. 599–600).

31. Borrower witness Mr. Richardson testified that he once collected on loan insurance (Tr. 656) and that for 8–10 years had always taken out insurance on his loans (Tr. 656–57, 673–74). He said he thought he had to have insurance but that he did not read the loan agreement papers (Tr. 658, 663–64, 669, 674, 677) although he could have (Tr. 658). He did not testify that an employee had led him to believe that insurance was required.

32. Borrower witness Mr. Martin at one point said that he had the impression that he had to have insurance (Tr. 696) and knew that he, in fact, did have it (Tr. 701). Mr. Martin also said he could have read the documents he was signing (Tr. 704, 706) but that he did not (Tr. 713) and that he learned the insurance was optional by reading the loan papers later (Tr. 696–98). Lastly, Mr. Martin testified that on a

subsequent loan he had with USLIFE Credit he decided against having insurance coverage (Tr. 708). He too did not testify that an employee had led him to believe that insurance was required.

33. Borrower witnesses Mrs. Grant and her husband testified that they did not read the loan papers (Tr. 740, 760–61), were not rushed (Tr. 741–42, 765) and were in a hurry to get the loan proceeds and leave the loan office (Tr. 755, 760, 765–66). They also did not testify that an employee had led them to believe that insurance was required.

34. To the same end, a former employee, Mr. Stricklen, who was called by complaint counsel, said that insurance was optional (Tr. 236), signed a statement which is in evidence to that effect (RX 22) and said that he explained the terms of loans to USLIFE Credit customers to the best of his ability (Tr. 242; RX 22). He also said that if a borrower refused insurance, he would refer the matter to his supervisor, a Mr. Daniels (Tr. 242). Similarly, a former employee, Mr. George, who also was called by complaint counsel, testified that he explained the loan terms, including a discussion of insurance on *new* loans and that insurance was automatically included on a loan renewal *if* the previous loan had insurance coverage *and* the borrower indicated that "everything would be the same, the same length of contract, the same insurance . . ." (Tr. 263–64). He said that he asked new borrowers who they wanted as the beneficiary of the insurance (Tr. 252) and informed them that the insurance was not mandatory (Tr. 252–53). Another ex-employee called by complaint counsel, Mr. Dionne, testified that insurance was presented as an option by respondents but that he did not personally offer it as an option (Tr. 789–90), [21] that not all loans were covered by insurance (Tr. 790), that borrowers had time to read the contract (Tr. 791) and that its terms were "gone over" (Tr. 791).

35. The one employee called by counsel for respondents, Mr. Miles, testified that borrowers were asked whether they wanted insurance (Tr. 857, 861, 867–68), that the terms of the loan were gone over with the borrower in the course of telephone conversations (Tr. 860), that he would try to sell insurance on the loan to the borrower (Tr. 862), that the borrower was not rushed to sign the loan papers, although marks were sometimes used to indicate where signatures were to be affixed (Tr. 865), and that his employer's instructions to him were that borrowers were to be informed as to all the terms of their loans (Tr. 865).

36. In view of this testimony, plus documentary exhibits in the record, the evidence is convincing that neither devious nor deceptive tactics or practices were utilized by respondents to induce borrowers to incur insurance charges when loans were taken out. It is established that loan documents were sometimes prepared in advance of the

borrower's visit to the office (Stricklen, Tr. 224–25) on the basis of information obtained over the telephone, but it is not established that this practice was improper or to the detriment of the borrowers. It is undisputed that respondents have adequate written disclosures on their loan agreements (CCPF, p. 30).

INTERSTATE COMMERCE NEED NOT BE PROVEN IN A TRUTH IN LENDING CASE

Section 108(c) "Administrative Enforcement" of the Truth in Lending Act (15 U.S.C. 1601, *et seq.*) provides that a violation of that Act is also a violation of the Federal Trade Commission Act (15 U.S.C. 41, *et seq.*) "irrespective of whether that person [who is in violation] is engaged in commerce or meets any other jurisdictional test in the Federal Trade Commission Act." Consequently, in order for Commission jurisdiction to attach, it is not essential that USLIFE Credit and USLIFE be engaged in or that their acts or practices affect interstate commerce as is required by the Federal Trade Commission Act, as amended by the Magnuson-Moss Warranty-Federal Trade Commission Improvement Act (15 U.S.C. 2301). The evidence adduced as to the character of the operations of USLIFE Credit and USLIFE in various states, however (Finding 3), establishes that they and the acts and practices called into question by the complaint, in fact, were in or affect interstate commerce. [22]

NAMING USLIFE AS A RESPONDENT

The evidence established that USLIFE, the parent corporation properly was named as a respondent. The chairman of the board of directors for USLIFE and its subsidiary, USLIFE Credit, was the same person (Finding 8). Proposed acquisitions by the subsidiary required and require approval by the parent (Finding 5). The parent also had/has veto authority over a decision by USLIFE Credit to close a branch office (Finding 5). Such involvement in the affairs of USLIFE Credit by USLIFE is sufficient evidence of control to warrant holding the parent liable for the acts and practices of the subsidiary. In *North American Co.* v. *S.E.C.*, 327 U.S. 686, 693 (1946), the Supreme Court said that:

> . . . ties and associations, combined with strategic holdings of stock, can on occasion serve as potent substitute for the more obvious modes of control. See *Southern Pacific Co.* v. *Bogert*, 250 U.S. 483, 491–492; *Natural Gas Co.* v. *Slattery*, 302 U.S. 300, 307–308. Domination may spring as readily from subtle or unexercised power as from arbitrary imposition of command. To conclude otherwise is to ignore the realities of intercorporate relationships.

To the same end, Commission precedents hold that in determining liability the "pattern and frame-work of the whole enterprise" is to be examined. See *Art National Mfrs. Distr. Co.* v. *F.T.C.*, 298 F.2d 476, 477 (2d Cir. 1962), *cert. denied*, 370 U.S. 939 (1962), citing *Goodman* v. *F.T.C.* 244 F.2d 584, 601 (9th Cir. 1957). The parent is vicariously liable for its subsidiaries' acts ". . . if the facts demonstrate even latent control." See *In the Matter of Beneficial Corporation and Beneficial Management Corporation*, CCH [1973–1976 Transfer Binder] Trade Reg. Rep. ¶ 20,959 at 20,812 (FTC 1975) [86 F.T.C. 119]. Previously, in its decision in *P. F. Collier & Son Corp.* v. *F.T.C.*, 427 F.2d 266, 270 (6th Cir. 1970) the court in upholding a Commission decision said:

> . . . [W]here a parent possesses latent power, through interlocking directorates, for example, to direct the policy of its subsidiary, where it knows of and tacitly approves the use by its subsidiary of deceptive practices in commerce, and where it fails to exercise its influence to curb illegal trade practices, active participation by it in the affairs of the subsidiary need not be proved to hold the parent vicariously responsible. Under these circumstances, complicity will be presumed.

[23] In its more recent *Beneficial* opinion, *supra*, at 20,814, the Commission specifically rejected the common law rule that corporate identities are to be observed unless the subsidiary is the mere tool of the parent and its separate identity is a mere fiction.

Where the public interest is involved, as it is in the enforcement of the Truth in Lending Act, a strict adherence to common law principles is not required in the determination of whether a parent should be held for the acts of its subsidiary when such adherence would enable the corporate device to be used to circumvent the policy of a statute. *Goodman, supra*, 244 F.2d at 591; *Joseph A. Kaplan & Sons, Inc.* v. *F.T.C.*, 347 F.2d 785, 787 n.4 (D.C. Dir. 1965).

Where the parent company is shown to be accountable for the acts and practices of its subsidiaries because of the latent power to control, which is the situation here, it is unnecessary to demonstrate that the practices of the subsidiary alleged to be illegal were expressly authorized by the parent *or* that the parent actively participated in them. See *P. F. Collier & Son Corp.* v. *F.T.C.*, *supra*, 427 F.2d at 270.

Conduct within the actual or apparent scope of authority of local managers and other employees subjects both the parent and the subsidiary to the jurisdiction of the Commission. See *Goodman, supra*, 244 F.2d at 592; see also *Parke, Austin & Lipscomb, Inc.* v. *F.T.C.*, 142 F.2d 437, 440 (2d Cir. 1944). Lastly, it should be mentioned that unsuccessful attempts to prevent misrepresentations by authorized agents will not put the principal beyond the reach of the Federal Trade Commission Act. *Goodman, supra*, 244 F.2d at 592. Thus the evidence establishes and judicial precedents support the naming of USLIFE as a respondent.

RELIANCE ON A TRUTH IN LENDING THEORY VIS-A-VIS PROVING A VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

The complaint charges that the alleged violations of the Truth in Lending Act by respondents constitute violations of the Federal Trade Commission Act (Complaint, ¶ One and ¶ Eight). Such charges are in accord with the provisions of Section 108(c) of the Truth in Lending Act that ". . . a violation of any requirement imposed under this title shall be deemed a violation of a requirement imposed under that [the Federal Trade Commission] Act." [24]

The evidence establishes that in spite of respondents' compliance with the written disclosure requirements of the Truth in Lending Act and employees "going over" loan terms with borrowers, some of the borrowers were still under the impression that insurance coverage was mandatory (*e.g.*, Ferrari, Richardson, Martin; Findings 30–32). Consequently, it appears that the disclosure practice respondents use could be improved upon. For example, the loan application form (RX 7) does not contain space for an entry to indicate the borrower's wish, or preference as to insurance coverage, although the loan agreement form (*e.g.*, RX 32) does contain such spaces. (See pp. 14a-b, 15d hereof.)

Evidence as to the failure to make disclosures, as to impressions created or as to the office setting in which a transaction is consummated may be sufficient to serve as the basis for findings that respondents were not making adequate disclosures regarding the optional nature of insurance, if proof of a violation was predicated on the theory that Section 5 of the FTC Act had been violated. There is ample precedent for the proposition that a violation of the FTC Act may be shown by evidence establishing that there has been inadequate disclosure of information which would enable consumers to make an informed choice. See *Pfizer, Inc.*, 81 F.T.C. 23, 58 (1972), citing in n.2 and n.3, *F.T.C.* v. *Colgate-Palmolive Co.*, 380 U.S. 374 (1965) and Gelhorn, "Proof of Consumer Deception Before the Federal Trade Commission," 17 Kansas L. Rev. 559 (1969).

The record reflects, however, that reliance on an FTC Act violation theory was specifically disclaimed on at least two occasions by complaint counsel (PHC, Tr. 30–31, 95–98). Under these circumstances, it would be a substantial deprivation of respondents' rights of due process to hold that the Federal Trade Commission Act had been violated when a violation of the Truth in Lending Act has not been proven. It is well settled that a change in theories in midstream may not be made without giving respondents reasonable notice of the

change. *Rodale Press, Inc.* v. *F.T.C.*, 407 F.2d 1252, 1256 (D.C. Cir. 1968), citing *N.L.R.B.* v. *Johnson*, 332 F.2d 216, 219–20 (6th Cir. 1963); *N.L.R.B.* v. *Fletcher Co.*, 298 F.2d 594 (1st Cir. 1962).

The Administrative Procedure Act, Title 5 U.S.C. 554(b), provides that respondents must be informed of "the matters of fact and law asserted" and there are judicial precedents holding that, if the party proceeded against understood the issues and was given the opportunity to defend himself, he has been accorded due process. See *Golden Grain Macaroni Co.* v. *F.T.C.*, 472 F.2d 882, 885 (9th Cir. 1972). In *Golden Grain*, at 886, the appellate court held that ". . . all facts relevant to [25] the alleged unlawful acts were fully litigated." In contrast, the evidence presented in these proceedings in the course of the case-in-chief and case-in-defense focused on, and was limited to, the requirements of the Truth in Lending Act. Complaint counsel said, in effect, that the Federal Trade Commission Act allegations hinged-upon and were consequential to the Truth in Lending charges.

Counsel for respondents specifically raised the question as to whether the provisions of the Federal Trade Commission Act were being relied upon and complaint counsel made it clear that no such reliance was intended. In this context, since the evidence adduced did not establish that the Truth in Lending Act had been violated, either explicitly or implicity, that evidence is insufficient to establish that the Federal Trade Commission Act had been derivatively violated, particularly in view of the evidence and agreement of counsel that the forms used by respondents *do* comply with the provisions of the Truth in Lending Act (Findings 28, 36).

As the case-in-chief was presented, the Truth in Lending predicate to the theory of the case was made clearer; respondents were apprised more specifically as to the acts and practices being challenged and had an opportunity to present their defense. Respondents did so successfully and may not now be held to have violated the Federal Trade Commission Act.

CONCLUSIONS OF LAW

The Federal Trade Commission has jurisdiction over the respondents and the subject matter of this proceeding.

These proceedings and the order issued hereby are in the public interest.

Respondents are in competition with other finance companies which lend money to the public.

Respondent USLIFE, the parent corporation, is vicariously responsible for the acts and practices of USLIFE Credit, one of its subsidiary corporations.

The evidence does not support the charges that respondents have or that they are violating the Truth in Lending Act. [26]

It would be a denial of due process to predicate a finding of violation of the Federal Trade Commission Act on this record.

ORDER OF DISMISSAL

It is ordered, That the complaint in this matter be, and it is hereby, dismissed.

OPINION OF THE COMMISSION

BY CLANTON, *Commissioner:*

I. BACKGROUND

On September 26, 1975, the Commission issued a complaint against respondents USLIFE Corporation (hereafter "USLIFE") and its subsidiary, USLIFE Credit Corporation (hereafter "USLIFE Credit") alleging violations of the Truth in Lending Act (15 U.S.C. 1601, *et seq.*), Regulation Z (12 C.F.R. 226) and the Federal Trade Commission Act (15 U.S.C. 41, *et seq.*). The issues at stake here concern the sale by USLIFE Credit of credit life and credit disability insurance in connection with its consumer loan business.

The complaint alleges that respondents violated Section 226.4(a)(5) of Regulation Z by engaging in acts and practices which operated "to defeat the elective language of the insurance authorization disclosures by obscuring from consumers knowledge about the [insurance] option." (Complaint para. 5). More specifically, the following practices were cited as illustrative of those which defeated the optional selection of insurance: [2]

(1) oral quotation of monthly repayment figures that include insurance charges;

(2) automatic inclusion of insurance charges in loan agreement papers;

(3) placement of an "X" at the appropriate signature line on the insurance authorization form prior to obtaining the customer's selection of insurance;

(4) failure to inform consumers as to the purposes of their signatures; and

(5) inclusion of charges for insurance in the "records of disbursements" section of the loan agreement without adjusting the finance charge and the annual percentage rate. (Complaint, para. 4)

The administrative law judge (ALJ) issued his decision dismissing the complaint on January 27, 1977. Having found that respondents' official policy was not to require insurance (ID 10,15),[1] the ALJ concluded that the practices utilized by respondents did not run afoul of the credit statute or its implementing regulations. In particular, the law judge found that respondents' employees were instructed to explain loan terms to customers and to avoid oral quotations which included insurance. (ID 14,16) He determined further that insurance was not automatically included in loan forms prior to customer authorization, borrowers were not pressured into signing the forms, and respondents did not otherwise thwart consumers' opportunity to read over the relevant forms. (ID 18,19) Finally, the judge found that use of "Xs" and other similar marks on the signature lines served as a convenience to customers in finalizing the loan agreement, rather than creating the impression that insurance was obligatory. In sum, the ALJ found no basis for concluding that respondents' acts or practices were responsible for any impression prospective borrowers may have had that insurance was required. (ID 30) [3]

The ALJ reached this decision after striking the testimony of seven complaint counsel witnesses pursuant to his interpretation of the Jencks Act (18 U.S.C. 3500). (ID pp. 5-9) Relying on *voir dire* testimony of these witnesses, the judge noted that Jencks Act statements may have been made but a conclusive determination would require examination of the handwritten notes of the Commission's investigator which complaint counsel were unable to produce.

While finding no liability, the ALJ ruled that it would be proper to hold USLIFE responsible for the acts and practices of its subsidiary, USLIFE Credit, citing the fact that the same individual served as Board Chairman of the two corporations and the parent's authority to review and approve certain decisions of its subsidiary. (ID pp. 22-23)

Complaint counsel appeal from the law judge's determinations on liability and the Jencks Act while respondents cross appeal on the question of parent liability. For the reasons set forth below, we reverse the ALJ's rulings pertaining to the Truth in Lending Act violations and the Jencks Act and uphold his determination concerning the liability of USLIFE.

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[1] The following abbreviations will be used in this opinion:

ID — Initial Decision finding no.
ID p. — Initial Decision page no.
Tr. — Transcript page no.
CX — Complaint counsel's exhibit no.
RX — Respondent's exhibit no.
RAB — Respondent's appeal brief
CAB — Complaint Counsel's appeal brief
R.Ans — Respondent's answering brief
C.Ans — Complaint Counsel's answering brief
TROA — Transcript of Oral Argument before the Commission

II. THE REQUIREMENTS OF THE TRUTH IN LENDING ACT

Section 226.4(a) of Regulation Z, which prescribes the manner for calculating the finance charge, specifies that it consists of all direct or indirect charges imposed by the creditor "as an incident to or as a condition of the extension of credit," including:

> (5) Charges or premiums for credit life . . . insurance, written in connection with any credit transaction unless:
>
> (i) the insurance coverage is not required by the creditor and this fact is clearly and conspicuously disclosed in writing to the customer; and [4]
>
> (ii) any customer desiring such insurance coverage gives specifically dated and separately signed affirmative written indication of such desire after receiving written disclosure to him of the cost of such insurance.[2]

Respondents contend that since the general purpose of the Act and Regulation Z is to insure uniform disclosures, and not to serve as an "antifraud" statute, no violation will lie if the creditor's policy is to make insurance[3] coverage optional and the policy is disclosed in writing [5] to customers. (R.Ans at 5–8)[4] We reject such a restrictive interpretation of the statute.[5] The issue here relates not to respondents' official policy, or the adequacy of their written disclosures, but to whether certain practices utilized by respondents effectively prevented consumers from exercising a free and knowing choice as to their insurance option. That is, despite respondents' official policy, have they engaged in practices that serve to obscure or defeat this policy, including the written disclosures contained in their loan agreements?

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[2] Section 226.4(a)(5) of Regulation Z implements the requirements of the Truth in Lending Act. Section 106(b) of the Consumer Credit Protection Act, 15 U.S.C. 1606(b) provides as follows:

> (b) Charges or premiums for credit life, accident, or health insurance written in connection with any consumer credit transaction shall be included in the finance charge unless
>
> (1) the coverage of the debtor by the insurance is not a factor in the approval by the creditor of the extension of credit, and this fact is clearly disclosed in writing to the person applying for or obtaining the extension of credit; and
>
> (2) in order to obtain the insurance in connection with the extension of credit, the person to whom the credit is extended must give specific affirmative written indication of his desire to do so after written disclosure to him of the cost thereof.

While the language of §106(b) of the Act and §226.4(a)(5) of the Regulation are slightly different, no issue is raised as to any possible inconsistency between the two provisions and we discern none. Accordingly, throughout the remainder of this opinion we will refer only to Regulation Z when discussing the alleged violation.

[3] Regulation Z, as it pertains here, encompasses several different types of insurance–credit life, accident, health, and loss of income. Since the legal and factual analysis is not altered by the particular type of insurance offered, we will merely make reference to "insurance" throughout this opinion without further specification of the particular type of insurance offered or selected.

[4] Of course, merely having an official policy that treats insurance coverage as optional will not suffice if the optional disclosure is itself so complex or confusing that the average consumer could not understand it. *Woods* v. *Beneficial Finance of Eugene*, 395 F. Supp. 9 (D. Ore. 1975); *Hall* v. *Sheraton Galleries of Atlanta*, 4 Cons. Cred. Guide (CCH) ¶ 98,737, (M.D. Ga. 1974). However, that issue is not before us here since no allegation has been made concerning the readability of respondents' written disclosures.

[5] The ALJ also rejected respondents' theory as well (ID 29), as did the original law judge assigned to this case (Judge Needelman) in his Memorandum and Order Respecting Respondents' Motion for Summary Decision, February 9, 1976.

Legislative and judicial authorities alike convince us that, notwithstanding a creditor's official policy to the contrary, a further examination of the creditor's practices is in order to establish whether the insurance election has been undermined and the statute violated. The significance of the written disclosure of insurance costs is emphasized in the regulations and elaborated upon in the following excerpt from the Conference Report on the Truth in Lending Act:

> Under the conference substitute, such [insurance] charges may not be excluded [from the finance charge] unless the coverage of the debtor by the insurance is not a factor in the approval by the creditor of extension of credit, *and this is clearly disclosed to the debtor. The creditor must also disclose to the prospective debtor the cost of such insurance, and may not include it in the financing package unless the debtor gives specific affirmative written indication of his desire to have it.* If . . . insurance is written in connection with any consumer credit transaction, without complying with all of the foregoing requirements, then its cost must be included in the finance charge. . . .[6] (emphasis supplied)

[6] As the underscored language indicates, more than pro forma compliance with the statute is called for. Both the optional nature and cost of the insurance must be clearly disclosed and, *before* including insurance in the loan agreement, the creditor must obtain the consumer's written authorization. During debate in the House on the Conference Report, the floor manager of the bill, Congresswoman Lenore Sullivan, reinforced the importance of preserving consumer choice in deciding whether to purchase credit insurance:

> In the final bill, credit life insurance is included in the finance charge if the consumer does not have a free opportunity to decide whether he wants the coverage, or if the insurance is a factor in the extension of credit.[7]

Thus, even if insurance is not a factor in the creditor's decision to extend credit, insurance costs will be included in the finance charge provided the consumer does not have a "free opportunity" to exercise his or her choice. The result is the same whether the creditor officially requires insurance coverage or informally does so through practices which undermine the would-be borrower's voluntary election. Surely, a determination as to whether the choice was truly "free" contemplates an inquiry into the facts and circumstances surrounding the credit transaction.

The cases also support this view. In *F.T.C.* v. *Jorgensen*, 4 Cons. Cred. Guide (CCH) ¶98,594 (D.D.C. 1975), the court dismissed out of hand a creditor's claim that a Commission inquiry into the practices surrounding the use of an insurance authorization form would amount to an ad hoc amendment to Regulation Z. The court held that "Regulation Z would be meaningless indeed if its requirements could be met in form and ignored or overridden in practice. An inquiry into actual practice is therefore appropriate." (*Id.* at 88,105.) Likewise, in *Fisher* v. *Beneficial Finance Co. of Hoxsie*, 383 F.Supp. 895 (D. RI 1974), the court observed that while a consumer's mere allegation that insurance was mandatory was insufficient to support a motion for summary judgment in her favor, she was free to introduce evidence at trial "that the defendant by its conduct did actually require . . . insurance to be purchased as a condition of [the] loan." (*Id.* at 900.) [7]

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[6] Conf. Rep. No. 1397, 90th Cong., 2d Sess. 25 (1968).

[7] 114 Cong. Rec. 14387 (1968).

Finally, we take note of the Federal Reserve Board's own interpretations of Section 226.4(a)(5)[8] In addressing specific requests for advice on proper application of this provision, the Board's staff has advised, for example, that even where insurance is officially labeled "optional," the practice of including insurance costs in the loan papers prior to obtaining the consumer's approval would have "the practical effect of precluding the customer's free exercise of choice as to whether he wishes the insurance. Without that choice Congress specified that the premiums would have to appear in the finance charge."[9] [8] In fact, evidence of such a practice alone might be sufficient to establish liability. Clearly, other practices surrounding a credit transaction, in addition to those cited by the Federal Reserve Board, are also integral to a proper assessment of the voluntary nature of the insurance option and should be examined.[10]

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[8] An agency's interpretation of its own rules and regulations is entitled to great weight in determining the purpose and application of those rules and regulations. *Griggs* v. *Duke Power Co.*, 401 U.S. 424, 433–434 (1971).

[9] FRB Letter No. 398 (August 26, 1970), [1969–1974 Transfer Binder] Cons. Cred. Guide (CCH) ¶ 30,576. *See also* FRB Letter No. 408 (September 14, 1970), [1969–1974 Transfer Binder] Cons. Cred. Guide (CCH) ¶ 30,586.

There is some hint in the court's decision in *Fisher* v. *Beneficial Finance*, *supra* at 900, that FRB Letter No. 408 supercedes the interpretation in FRB Letter No. 398. In fact, a close reading of the two letters shows them to be perfectly consistent. In Letter No. 398, the staff expressed its view that a "separate disclosure" of the cost of insurance prior to the consumer's election was the best method for insuring that the election was knowingly made. It was further noted that his "separate disclosure" should appear on the insurance authorization form itself.

Letter No. 408 reiterated this view but counseled the requester that the staff did not intend to imply that disclosure on the authorization form itself was the only method by which compliance could be achieved. The staff advised that if the creditor could prove that the disclosure was actually made before the consumer's election, §226.4(a)(5) would be satisfied. Significantly, though, the staff did not back away from its advice in Letter No. 398 and suggest that incorporation of the insurance charges within the terms of the loan agreement would be a permissible method of disclosure.

[10] To the extent that *Stanley* v. *Evan Motors*, 394 F.Supp. 859 (M.D. Fla. 1975), and *Mims* v. *Dixie Finance*, 426 F.Supp. 627 (N.D. Ga. 1976), two cases cited by respondents, indicate the contrary, we respectfully decline to follow them. In both cases, consumers alleged that insurance was required by the creditor but introduced no extrinsic evidence that would contradict the duly signed insurance authorization form. Although the facts in those cases are distinguishable from the one before us, both courts appear to have placed great reliance on the mere fact that the authorization form was signed. For example, the *Mims* court, in reaching its conclusion, stated that the "plaintiff must prove that the creditor specifically and unequivocally informed her that insurance is required in order to contradict the recital to the contrary." 426 F.Supp at 631. Should such a standard preclude proof of the type offered here, we believe it is inconsistent with the intent of Congress and contrary to judicial and administrative interpretations which contemplate inquiry beyond "unequivocal" statements by the creditor.

Even if our interpretation were not so clearly expressed in the language and legislative history of the specific provision at issue here, the broader purpose of the Truth in Lending Act supports the proposition that a consumer's insurance choice must be freely and knowingly exercised before the costs can be excluded from the finance charge and the annual percentage rate. There is no doubt, and the parties agree, that the Act was fashioned to enhance the accuracy of credit information available to consumers and to facilitate comparison shopping among the offerings of different creditors.[11] Congress recognized that consumers were woefully ignorant of the costs and consequences of their credit choices, a situation produced in large measure by divergent, and sometimes fraudulent, practices which obscured the differences and real costs of available credit terms.[12] In striving to promote uniformity and simplicity, Congress relied heavily upon the annual percentage rate. As Senator Proxmire, the bill's principal sponsor in the Senate, stated: **[9]**

> [T]he bill would require that in most forms of credit the creditor would disclose the annual percentage rate. This is the universal common denominator by which the cost of money is measured. It permits a consumer to readily compare the cost of credit among different lenders regardless of the length of the contract or the amount of the downpayment. In effect, the annual percentage rate is a price tag for the use of money.[13]

Moreover, Congress realized that the utility of this "price tag" indicator would be severely eroded if creditors were free to eliminate from the costs of extending credit a variety of charges and fees that were actually conditions and terms upon which the credit would be extended—a practice Congress found to have occurred with some frequency.[14] Accordingly, the Act specified the types of additional and extraordinary fees and charges, including insurance, that must be included in the finance charge and reflected in the annual percentage rate.

The scheme established by Congress, with its reliance on the annual percentage rate, demands careful adherence to the principle that insurance costs must be reflected in the annual percentage rate unless such costs are made wholly optional. Where insurance is required, it must be treated as a cost of the credit since it automatically becomes part of the credit transaction. Where it is optional, it can be eliminated from the cost of credit but only because the consumer has been informed of its separate cost and has had full opportunity to accept or reject it. Were creditors free to manipulate their insurance costs, Congress' goal of preserving the comparability of credit offerings would be readily defeated. Given the sensitive nature of the annual percentage rate as a cost-of-credit barometer, it strikes us that the Congressional purpose can be achieved only if Section 226.4(a) is construed to require the inclusion of insurance costs in the finance charge whenever insurance is not truly voluntary. [10]

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[11] One need go no further than Congress' statement of intent embodied in Section 102 of the Act (15 U.S.C. §1602) which states that the purpose of the Act is "to assure a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him and avoid the uninformed use of credit. . . ." *See also* CAB at 16–17 and R.Ans at 8–14.

[12] H.R. Rep. No. 1040, 90th Cong., 1st Sess. 10–13 (1967); S. Rep. No. 392, 90th Cong., 1st Sess. 1–3 (1967).

[13] 113 Cong. Rec. 18400 (1967).

[14] H.R. Rep. No. 1040, *supra* at 13; S. Rep. No. 392, *supra* at 3.

Given the remedial nature of the Truth in Lending Act, it is entitled to be liberally construed in order to assure that its objectives are met in form as well as in substance.[15] As such, it is entirely appropriate that the Commission inquire into the acts and practices surrounding the credit transactions at issue here to ascertain whether respondents' official policy with regard to insurance was implemented in fact as well as in theory. [11]

III. RESPONDENTS' PRACTICES

A. *Insurance Election*

There is no dispute that USLIFE Credit's official policy provides that insurance is optional (ID 10; RX 2,3) and that this policy was appropriately embodied in each credit contract by inclusion of a written notice disclosing the optional nature of the insurance. (ID 12, p.15d) Indeed, by operation of law in 19 of the 20 states in which USLIFE Credit does business, the company is prohibited from requiring insurance. (Tr.80–81) As we have previously noted, however, such a policy alone does not suffice to absolve respondents from liability under TILA. A further examination of respondents' practices, therefore, is in order to determine respondents' compliance with the statute.

In the typical loan transaction, the consumer would contact USLIFE Credit, either by phone or in person, to inquire about the possibility of obtaining a loan. Respondent's personnel would ascertain the purpose, amount needed, and other data necessary to determine credit worthiness. After appropriate credit checks, the loan office would call back to confirm whether the loan would be granted and, if so, to obtain further information for processing the required documents. Once approved, the consumer was invited to come into the appropriate USLIFE credit office to finalize the transaction. (Tr.860–63, TROA 27–

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[15] *See e.g., Mirabel* v. *General Motors*, 537 F.2d 871,878 (7th Cir. 1976); *Rachbach* v. *Cogswell*, 547 F.2d 502,505 (10th Cir. 1976); *Johnson* v. *McCrackin-Sturman Ford*, 527 F.2d 257,262 (3d Cir. 1975); *Littlefield* v. *Flanagan & Co.*, 498 F.2d 1133,1136 (10th Cir. 1974); *Eby* v. *Reb Realty*, 495 F.2d 646,650 (9th Cir. 1974).

29) At this final visit the loan papers, including insurance authorization forms, were signed.

The complaint charges that respondents engaged in a variety of practices which had the effect of defeating the voluntary insurance election. Among others, these include: (1) quoting monthly repayment figures to consumers which include insurance, (2) automatically including insurance charges on the loan agreement and disclosure papers presented to consumers for signature, (3) marking an "X" by the signature line reserved for authorization of insurance without permission of the borrower, and (4) presenting pretyped loan agreements to consumers for signing without disclosing the purpose of the signatures.

Respondents do not dispute that repayment terms are quoted which include insurance, or that loan documents containing insurance charges are prepared in advance of presentation to borrowers for signature and before they have received written disclosure of the insurance option. [12] Rather, they contend that such actions are not taken without first informing customers that insurance is voluntary and obtaining their consent. Similarly, respondents argue, and the ALJ agreed, that showing customers where to sign by "X"s or otherwise is merely a convenience to assist them in signing on the proper line after exercising their option to purchase insurance. Respondents also assert that the terms of loans, including insurance charges, were explained to customers before signing.

Further, even if there were deficiencies in their practices, respondents emphasize that those problems were cleared up before they learned of the Commission's investigation in 1973. To support that contention, respondents point to a directive circulated to all branch offices on June 22, 1973, which established "policies and procedures that will insure full compliance with the letter and spirit of the Truth in Lending laws and regulations." (RX 2) Among other things, that directive instructed loan personnel to: (1) clearly indicate the voluntary nature of insurance when quoting loan repayment figures which include such charges, (2) explain the insurance options to the customer before typing up the loan papers, (3) avoid indicating by an "X" or other mark which insurance option the customer should sign, since "[t]he choice must be a free act on the customer's part," and (4) promptly retype the loan documents where the customer's "signed election" differs from "his initial election."

Turning to the first complaint allegation, the record indicates quite clearly that monthly repayment figures were quoted which include the cost of insurance. (Answer to Complaint pp. 5–6) But, as respondents point out (R.Ans at 31–32), the significance of this practice in terms of its potential for consumer deception is less obvious. More relevant to our inquiry is what, if anything, consumers were told about insurance *before* it was incorporated into loan agreements and *before* they received written disclosure of their insurance options.

In connection with the advance preparation of loan documents which include insurance, we are unable to agree with respondents and the ALJ that this practice was wholly innocuous. Although such action may at times have been preceded by oral disclosures that insurance was optional (Tr.863), there is considerable evidence that in many instances the disclosures were inadequate or non-existent.

For example, Mr. Dionne, former manager of respondents' Houston office, testified that he did not present insurance as an option on renewal loans. In elaborating on his response for the ALJ, Mr. Dionne stated: [13]

> Did I present [insurance] as an option, no sir, I did not, that's the thing . . . nor did any other individual who may have been closing a loan when the information would be taken over the phone or whatever . . . . (Tr.790)

Similarly, Mr. Basil George, another former branch office manager for USLIFE Credit, indicated that "[o]n a renewal loan [insurance] was automatic." (Tr.263) At most, the customer was asked whether everything would be the same, but it was "automatically assumed they would want the insurance." (Tr.264) Witness Stricklen provided further confirmation that in the case of renewal loans consumers were not generally informed about their insurance options before the charges were incorporated into the loan agreements. (Tr.221–24)

Even with respect to new loans, it appears that customers often were not informed about the insurance election before closing. On cross-examination, Mr. George observed that new customers were "[n]ot always" informed that insurance is not required. (Tr.253) According to him, those that called in to apply for a loan were told only what the insurance charges would be, while those who came into the office were urged to take insurance but informed that it wasn't necessary. (Id.) No reason is given for this different treatment.[16] [14]

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[16] Respondents, in an attempt to undercut the testimony of Messrs. Stricklen and George, introduced statements signed by both which were obtained prior to trial. (RX 22,23) These statements, which were drafted by respondents' counsel, carefully sidestep whether the voluntary nature of insurance was explained to customers before preparation of the loan papers. The statement by Mr. George, for example, that in the case of renewal loans "it was more likely that the insurance would be taken for granted" is clearly consistent with his testimony. As for new loans, the statement merely notes that insurance was explained with each loan without describing exactly what was said. Only at the end does the statement suggest that USLIFE Credit's policy was to inform customers that the purchase of insurance was up to them, though they were advised to take it.

Similarly, the prepared statement signed by Mr. Stricklen indicates that insurance charges were explained to customers before closing, usually on the loan application itself. Yet, as the record reveals, nowhere on the loan application is there any mention that insurance is voluntary. (ID pp. 14a–b) As for telling customers at closing that insurance was not mandatory, Mr. Stricklen explained at trial that he did so by simply pointing to the insurance signature lines and asking the customer for his or her signature, a practice hardly calculated to overcome the effects of

(Continued)

Further, witnesses Stricklen and George, who were both supervised by the same regional manager, testified that they were under standing orders not to make loans without insurance. (Tr.220,264) Mr. George stated that if a customer refused insurance, he would have to call his supervisor and get approval. (Tr.264) To avoid telling customers that insurance was required, other tactics were used, such as advising them that "the company's policy was we like to have insurance on every loan. . . ." (Tr.252) Those efforts were apparently quite successful since Mr. George acknowledged that he could not recall any instance where insurance was not sold. (Tr.247,249–50)

Consumer testimony provides further corroboration that borrowers were not fully informed about their right to decline insurance before it was inserted in the loan agreement. (Tr. 648,69395, 72526) For example, consumer witness Rucille Grant, who had previously borrowed from respondents, testified that insurance was never mentioned, either during her initial call to arrange for the loan or when she went in to sign the papers and pick up the check. (Tr.725–26) Similarly, Mr. Richardson indicated that insurance was never discussed until closing when the loan officer went over the terms of the loan and read off that "the payment was so much and the insurance would be so much. . . ." (Tr.648) Mr. Martin was told only what the insurance was for and how much it cost. (Tr. 695)

Another witness, Laura Ferrary, testified that one of respondents' loan officials told her insurance was included in the loan agreement because it was required to get a loan (Tr. 572, 592–94). The ALJ chose to discount Mrs. Ferrary's testimony because she appeared "hostile toward respondents" for having made her feel foolish in asking whether the insurance was optional. (ID 30) There is also a conflicting account supplied by respondents' sole witness, Jeffrey Miles. But even if we credit his version, it only underscores the dangers in relying on oral disclosures to suffice as a basis for including insurance in the loan papers prior to closing. Mr. Miles, who was a manager-trainee in the branch office where Mrs. Ferrary's loan was handled, testified that when she initially came in to apply for the loan, she was told about the insurance and that it was optional. Yet when asked to explain why the insurance was inserted in the loan agreement, Mr. Miles responded as follows:

> A. We tell her that she has $150 worth of life and accident and health and she didn't say that she didn't want it.

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preparing loan documents in advance of closing which include insurance within the terms of the loan.

In short, these statements do not detract from the overall thrust of the testimony that many would-be borrowers had little or no knowledge that insurance was included in the loan agreement prior to signing.

Q. Would you answer my question? How did it come that insurance appeared on the loan agreement when she did not ask for the insurance, as you have testified?

[15] A. We asked her if she wanted the $150 with life and accident and health and she didn't say she didn't, so that's why we typed it on.

Q. Didn't you testify that she didn't ask for the insurance?

A. She didn't ask for it, but what I said is we told her that the loan was $150 — or I didn't tell her — Marty told her it was $150 with life and accident and health.

Such a conversation simply illustrates the shortcomings of oral disclosures and the likelihood that consumers will not be fully aware of their rights when agreeing to inclusion of insurance in the loan contract.[17] Moreover, once that initial decision has been made, subsequent written disclosures are much less likely to be effective.

This evidence, we believe, thoroughly substantiates the complaint's allegation that insurance was included in many loan documents prior to closing without the consumer's knowledge. At other times, insurance may have been discussed but borrowers were not aware that it was voluntary. In our view, such action is inherently inconsistent with the statutory scheme, which contemplates *written* disclosure of the insurance option and its cost *before* consumers make their choice. Even if consumers are informed at the outset that insurance is not required, oral disclosures are inherently unreliable, particularly where the lender, as here, has an economic stake in the sale of insurance. While there is obviously nothing improper in respondents engaging in the sale of credit insurance, such an interest only underscores the importance of assuring that the written disclosures are not undermined.[18]

[16] Respondents nevertheless contend that the practice involved here is merely a convenience to consumers who have already made their insurance selection orally during the first communication with respondents and that any potential for misunderstanding is cured by respondents' practice of "going over" the loan forms with the customer. (R.Ans 33–34) We concur, however, with the view expressed by the Federal Reserve Board that the prior preparation of forms with insurance included has the tendency to reduce, if not eliminate, the

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[17] We also note that Mr. Miles' account was based on a conversation which he overheard from an adjacent office when Mrs. Ferrary came in to apply for a loan. (Tr. 847–53) Respondents chose not to call the loan officials directly involved in handling this loan.

[18] The conflicting pressures facing respondents' employees are reflected in the testimony of Mr. Beckley, USLIFE Credit's Vice President for Operations. In explaining the advice communicated to loan personnel about the proper handling of credit insurance (*see* respondents' instructional bulletin, RX2) Mr. Beckley pointed out:

> "We wanted to make sure that our branch people continue to sell, and that means not only that he [sic] tells them what the advantages are and . . . what the benefits are of the program we are selling. We didn't want to send out a memorandum that was negative in context because we hadn't changed our policy. The execution of the policy was that they had to sell the insurance. They had to also obey the law." (Tr. 90)

likelihood that consumers will truly appreciate the options available to them and understand that insurance is not a required part of the transaction. As stated in a staff advisory letter,

> to permit disclosure only in the completed series of calculations perpetuates the practice of preparing all documents with the insurance included. This has the practical effect of precluding the customer's free choice as to whether he wishes the insurance.[19]

Indeed, unlike the ALJ (ID 16), we believe that "going over" already completed loan papers (which include insurance) is not an obvious benefit to consumers from the point of view of insuring full understanding of their insurance options. The mere reiteration of the amount of the insurance costs may serve to reinforce the notion in consumers' minds that insurance is part of the deal. (Tr.648, 695–96)[20] While concluding that a law violation had not been established, the law judge conceded [17] that "in spite of respondents' compliance with the written disclosure requirements of the Truth in Lending Act and employees 'going over' loan terms with borrowers, some of the borrowers were still under the impression that insurance coverage was mandatory . . . ." (ID p.24) He went on to add "that the disclosure practice respondents use could be improved upon" by setting forth, for example, the borrower's insurance options on the loan application forms. (Id.)

There is no doubt that more, rather than less, disclosure is preferable. But the problem with respondents' practices is not the absence of written disclosures but the fact they were made in many instances only after the insurance had been incorporated in the loan agreement. Moreover, providing for written disclosure of the insurance election on the application form does not address the situation where the necessary credit information is taken over the phone.

The ALJ draws additional support for his finding that TILA was not violated from evidence that respondents did not rush consumers into signing the final loan papers. On those occasions when consumers signed quickly, he concluded it was due to their own wish to complete the transaction expeditiously. (ID 18,19) As desirable as it may be to give consumers ample time to review the loan documents, the record reveals that such a practice, to the extent it was followed by respondents' employees, proved insufficient to negate the impression garnered by consumers that insurance was a factor in the loan transaction. That is not to say that all customers were misled by respondents' practices into believing that insurance was required. The record is clear that respondents were not able to sell insurance on every loan. Some customers obviously understood that insurance was voluntary and managed to resist respondent's inducement to purchase it. (CAB 40; Tr. 791) Nevertheless, in confronting completed loan papers which show that insurance coverage is included in the terms of the agreement, we believe it is not unreasonable for consumers to conclude that insurance is simply part of the transaction. In addition, as the record indicates, pointing out the insurance charges at closing may well strengthen that belief.[21] [18]

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[19] *See* FRB Letter No. 398, *supra*. The Commission has recognized as much in a related case brought under Section 5 of the FTC Act. In *Peacock Buick*, 86 F.T.C. 1532, 1558 (1975), *appeal denied*, 553 F.2d 97 (4th Cir. 1977), the Commission condemned the practice of filling out loan papers with insurance included prior to proper disclosure to consumers. While the degree of affirmative misrepresentation may have been greater in that case, the routine filling-in of insurance coverage by respondent was viewed as part of a course of conduct which further reduced the likelihood that the customer's insurance choice was truly optional. Moreover, there are other practices here which contribute to the misimpression conveyed by the prior inclusion of insurance in the loan agreement.

[20] Although the issue is not squarely before us, respondents' practices might well run afoul of §226.6(c) of Regulation Z which prohibits the disclosure of "additional information" that may "mislead or confuse customer . . . or contradict, obscure, or detract attention from the information required . . . to be disclosed." Thus, to the extent that information communicated during the "going over" process, or otherwise, tends to contradict, obscure or detract from the insurance authorization disclosure, §226.6(c) may be violated.

Respondents advance a further argument that no violation occurred because many of the loan transactions at issue here were "renewal" loans. (R.Ans 30) Since a customer has been through the routine before, he or she is already apprised of the optional nature of insurance and, presumably, immune to any misinterpretation caused by respondents' practices. Even assuming, however, that customers were aware of their options during the first loan transaction, it does not follow that consumers will inevitably want to extend insurance coverage to subsequent loans. Neither the Act nor Regulation Z makes any distinction between such loans and we see no compelling basis for applying less rigorous standards to renewal loans.[22] Indeed, given the fact that any deception or misunderstanding on an initial loan could readily carry over to renewal loans, there are sound policy reasons for treating each transaction in isolation.

In addition to the charge that insurance is included in loan documents before written notice is provided to customers, the complaint further alleges that respondents used marks ("X"s) to indicate where consumers were to sign for insurance. (Complaint para. 4(3)) A related allegation is that customers were asked to sign the insurance authorization portion of the loan agreement without disclosing the purpose of the signature. (Id. para. 4(4)) As the ALJ found, these practices occurred (ID 21,23) and respondents admit that marks were used, though they contend that such action merely served to assure that customers signed on the proper line after voluntarily deciding to purchase insurance. (R.Ans at 33)

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[21] Nor can respondents derive any solace from their adoption in 1975 of a 15-day (25 days in Illinois) cooling-off period during which a consumer could cancel his or her insurance selection and receive a full refund. (R.Ans 34) Having failed to assure that consumers receive written notification of their rights before insurance is put into the loan papers, respondents cannot rely on this *ex post facto* remedy to avoid the consequences of the statute and Regulation Z. Moreover, a cooling-off period is not a cure for the injury caused by deceptive sales inducements, since many consumers who have been led to purchase by deception are unlikely to discover the deception in time to take advantage of their right to cancel.

[22] *See Ives* v. *W.T. Grant*, 4 Cons. Cred. Guide (CCH) ¶98,561 (2d Cir. 1975).

While it is certainly appropriate, indeed desirable, for respondents to explain the loan documents to customers, it is quite another thing for respondents to suggest by marks or otherwise that the signature authorizing insurance is needed to complete the loan transaction. The record reveals that the practice of placing an "X" by the signature line or asking customers to "sign here" contributed to the belief of borrowers that insurance was a necessary part of the loan package. (Tr.698, 726) This practice, coupled with the prior preparation of loan papers containing insurance, prevented consumers from making a fully informed choice as to their insurance options.

Though obviously not dispositive of the liability issue, we note that respondents also have concluded that use of "X"s or other indicators may undermine a truly free selection by consumers. In a 1973 instructional bulletin to its own personnel, respondents condemned the practice and directed employees as follows: [19]

> Do not indicate by an "X" or any other mark, which of the insurance options the consumer is to sign. The choice must be a free act on the customer's part.[23]

Even if such practices might be harmless under other circumstances, they were not in this instance. As consumer testimony indicates, the signature markings or requests were initiated by respondents' loan officers rather than in response to a customer's expressed wish to purchase insurance. (Tr.726) Nor did "going over" the loan papers and charges, as we have already pointed out, prove effective as an antidote to cure previously established misconceptions.[24]

In sum, we believe there is ample evidence to conclude that respondents' conduct falls short of the requirements of the Truth in Lending Act and Regulation Z. Such a finding is warranted solely from respondents' inclusion of insurance in loan documents prior to giving consumers proper written disclosure of their options. Other practices, such as telling customers about credit insurance charges without disclosing that insurance is voluntary and asking customers to sign for insurance (through check marks or otherwise) before they have elected to purchase such coverage, contributed to borrower confusion about the voluntary nature of the insurance. These practices, independently and collectively, served to obscure and undermine the statutorily required disclosures. As a result, respondents' failure to include the cost of insurance in the calculation of the finance charge and annual percentage rate constitutes a violation of the credit statute and Section 5 of the FTC Act.[25] [20]

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[23] RX 2. The record indicates that, despite respondents' instructions, some branch offices continued to place marks by the insurance signature lines. (CX356-381)

[24] We also disagree with the law judge's suggestion that the absence of an "ulterior" motive exonerates respondents here. (ID 23) The closest the Act comes to recognizing intent is to provide in §105(c) that creditors will have a defense if they can show "by a preponderance of evidence" that the violation was "not intentional and resulted from a bona fide error notwithstanding the maintenance of procedures reasonably adopted to avoid" the violation. The defense, however, is only available in private suits and not in law enforcement actions brought by the Commission or other regulatory agencies.

Obviously, by our holding here we do not imply that respondents must guarantee that consumers fully understand the import of the written disclosures concerning their insurance options. Further, even with adequate disclosures, it is certainly possible that the vast majority of consumers, as respondents suggest, will still elect to purchase insurance.[26] What we do emphasize is that respondents must scrupulously avoid actions which undercut the importance of the written disclosures and render them meaningless. Where insurance charges are included in the loan papers prepared for closing, the likelihood that consumers will receive the full benefit of the subsequent written disclosures is greatly reduced. That is particularly true given respondents' desire to sell insurance and the reluctance by all parties to incur the delay associated with the preparation of new papers (or a check reimbursing the premium). In our view, both the express language and policy of the Truth in Lending Act require more. [21]

B. *Dating of Insurance Election*

As the ALJ found, insurance authorization forms signed by respondents' customers were not always separately dated. (ID 27) The law judge concluded, however, that the requirements of Regulation Z[27] were satisfied because the insurance authorization appeared on the same page of the loan agreement as the TILA disclosure statement which was dated.[28]

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[25] Respondents also argue that they cleaned up any problems which might have existed before the Commission began its investigation. It is clear, however, that respondents have not discontinued their practice of including insurance in the loan papers prior to closing. In addition, all the consumer testimony involved transactions which occurred after respondents issued their June 1973 notice (RX 2) to branch offices describing the procedures to be followed in selling credit insurance. *See also* note 23 *supra*.

[26] Although the high rates of insurance coverage revealed here–as much as 97 percent for credit life insurance (CAB at 39–40)–do not establish that respondents used deceptive means to sell insurance, these figures are not inconsistent with the finding that law violations have occurred.

[27] Section 226.4(a)(5) requires that insurance be included in the finance charge unless it is not mandatory and:

> "(ii) any customer desiring such insurance coverage gives *specifically dated* and separately signed affirmative written indication of such desire after receiving written disclosure to him of the cost of such insurance." (emphasis supplied)

[28] The ALJ apparently assumed that the date at the top of the loan agreement was the same as the date which otherwise would have appeared next to the signature line on the insurance authorization portion of the agreement. (ID 27)

Although the violation alleged here may be relatively minor in nature, we believe that the ALJ erred in his determination.[29] Section 226.4(a)(5)(ii) of Regulation Z provides that a customer's request for insurance coverage must be "specifically dated and separately signed." On its face, that language leaves little doubt that the insurance authorization itself must be signed and dated. Moreover, the Federal Reserve Board has consistently maintained that this provision calls for the insurance authorization form to possess a date block separate from that which appears elsewhere on the loan agreement.[30] This policy is reflected [22] in the sample forms used by the Board to illustrate compliance with Regulation Z[31] and respondents' own forms contain a separate date block, although they were not uniformly filled in. (CX 135–414)

The cases cited by the law judge (ID 27) and respondents (R.Ans at 53) are not necessarily inconsistent. In these decisions, which were handed down by the same court, *Porter* v. *Household Finance Corp. of Columbus*, 385 F.Supp. 336 (S.D. Ohio, 1974) and *In Re Warren*, 387 F.Supp. 1395 (S.D. Ohio, 1975), it was recognized that failure to provide a separate date next to the customer's insurance selection signature could lead to confusion and deception. Though noting its preference for separate dating, the court in each instance found that no violation had occurred since the plaintiffs stipulated that the date they selected insurance was in fact the same date which appeared at the top of the loan agreement. (385 F.Supp. at 345; 387 F.Supp. at 1404) In essence, the court found that no actual controversy existed.

Even if such a result is appropriate where private litigation is concerned, in public proceedings such as this one we do not believe complaint counsel should bear the burden of establishing that the date shown elsewhere on the loan agreement differs from the actual data consumers signed the insurance authorization. As the court in *Warren* acknowledged (387 F.Supp. at 1404), separate dating affords a means of ascertaining whether insurance was authorized before being included in the credit contracts. Allowing a date appearing on another part of the agreement to suffice as compliance with the provisions of Section 226.4(a)(5)(ii) would conflict with the very basis for the rule. The potential for confusion, should separate dating not be required, is highlighted by the fact that respondents' employees prepare the loan forms (and insert the date set for closing) some time prior to the consumer signing the insurance authorization. Given the specific language of Regulation Z and its interpretation by the Federal Reserve Board, we conclude that respondents have not fully complied with the requirement that the insurance election be separately signed *and* specifically dated by their customers. [23]

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[29] Respondents also contend that the absence of a date on copies of loan agreements introduced in the record does not establish that dates were missing from the originals. Since the loan papers introduced were obtained from respondents' files and no other questions as to their validity have been raised, we believe it reasonable to infer from the copies that the original documents were not properly dated.

[30] *See, e.g.*, FRB Letter No. 398, *supra* note 9. This policy has been reaffirmed in a recent FRB letter. In response to a request for advice on whether a credit union line of credit plan would comply with Regulation Z when the insurance disclosures and insurance authorization forms were delivered after approval of credit, the staff advised:

> Although the fact that insurance is not required is sufficiently disclosed, the other requirements of §226.4(a)(5)(ii) are not met because the customer has neither dated nor separately signed the insurance authorization. . . . Furthermore, in staff's view, the date on the front of the check and on the disclosure form do not constitute the specific date required by §226.4(a)(5)(ii). Staff believes that this would not suffice for two reasons. First, since the provision requires the authorization be '*specifically* dated,' the authorization itself must be dated. Additionally, since . . . the dates on the front of the check and disclosure statement are placed there by the creditor at the time of the mailing of the check, they will necessarily be different from the date on which the customer signs the authorization." (emphasis in original)

FRB letter No. 1103 (March 16, 1977), 5 CCH Cons. Cred. Guide ¶31556.

[31] *See* FRB Model Forms, Exhibits C & E, 1 CCH Cons. Cred. Guide ¶¶ 3853, 3855.

IV. LIABILITY OF USLIFE CORPORATION

Should a law violation be found, the ALJ concluded that it would be proper to hold USLIFE responsible for the acts and practices of its wholly-owned subsidiary, USLIFE Credit. In reaching his decision, the law judge looked to the following evidence:

— USLIFE and USLIFE Credit share the same individual as Chairman of both boards of directors. Two directors of USLIFE Credit are officers of USLIFE. One director of USLIFE Credit is an officer of USLIFE. (ID 6,7,8);
— USLIFE exercises control over the subsidiary's budget, has knowledge of USLIFE Credit's loan forms, and could order discontinuance of the forms (ID 5); and
— USLIFE Credit cannot purchase other companies or close a branch office without the parent's approval. (ID 5)

It is well established that the Commission is not bound by common law standards respecting separate incorporation of legal entities where such action will help to assure effective relief or otherwise fulfill statutory policies. *E.g., Zale Corp. and Corrigan-Republic, Inc.* v. *FTC*, 473 F.2d 1317 (5th Cir. 1973); *P.F. Collier & Son Corp.* v. *FTC*, 427 F.2d 261 (6th Cir. 1970), *cert. denied*, 400 U.S. 926 (1970); *Beneficial Corp.*, 86 F.T.C. 119 (1975), *aff'd in part and rev'd in part on other grounds*, 542 F.2d 611 (3d Cir. 1976), *cert. denied* 430 U.S. 983 (1977); *Jim Walter Corp.*, Dkt. 8986 (Dec. 20, 1977) [90 F.T.C. 671] That principle applies with equal force here even though USLIFE's relationship to its subsidiary and the acts and practices in question may be of a somewhat different order than existed in other cases.

The facts reveal that USLIFE, as a holding company, conducted its operations through a number of subsidiaries, including USLIFE

Credit, which ran its consumer credit business. (RX 21) USLIFE Credit was formed in 1970 to consolidate the operations of several consumer finance companies previously acquired by USLIFE. (Tr.209–10; RX 21) The credit subsidiary directs the affairs of approximately 220 branch loan offices in 20 states. (ID 3) [24]

Although there is nothing in the record to show that USLIFE participated in or had knowledge of the practices under challenge here, the parent plays a direct role in establishing and reviewing financial policies for its subsidiaries. Annual plans must be submitted by each chief executive officer (Tr.201) to USLIFE and specific objectives are then worked out jointly between the parent and subsidiary. (ID 8) Periodic reviews of USLIFE Credit's financial performance are conducted by Mr. Giuliano, who serves as both Executive Vice President of Financial Services for USLIFE and as director of the credit subsidiary. In addition, the policy coordination between the two firms is further reflected by the fact that Mr. Crosby is Chairman of the Board of both USLIFE and USLIFE Credit.

These circumstances convince us that it is appropriate to hold USLIFE responsible for the actions of its subsidiary. To be sure, as respondents argue on appeal (RAB at 18), virtually any parent-subsidiary relationship will evidence some of the indicia of ownership reflected in this record. While that may be true, we believe that where a parent has complete control over its subsidiary, even if such control is not fully exercised, there is a sound legal and policy basis for imposing accountability at a higher level in the corporate hierarchy. *See Beneficial Corp., supra,* 86 F.T.C. at 159. To the extent its subsidiary's unlawful conduct leads to increased sales of credit insurance, USLIFE reaps the benefits of enhanced profitability, a factor which in turn is reflected in the parent's financial statements. Thus, it hardly seems unfair to require USLIFE to exercise its unbridled power to control the conduct of its wholly-owned subsidiary.

Moreover, given the broad remedial purposes underlying the credit disclosure statute, it is especially important to ensure that compliance is achieved in a way which enhances self-enforcement and minimizes the need for repeated government intervention. That is particularly appropriate in situations like the present one where the corporate enterprise draws its sustenance from a multitude of subsidiary operations. That is not to suggest, as complaint counsel seem to imply (C.Ans at 3), that USLIFE has demonstrated a propensity for creating and dissolving corporations to avoid legal sanctions merely by acquiring several loan companies and merging them into USLIFE Credit. What it does suggest is that the reality of USLIFE's overall operations is such that future changes through acquisition, reorganization or otherwise could unduly restrict the application of an order running only to the credit subsidiary. In short, from the standpoint of effectuating the objectives of the Truth in Lending Act as well as fairness to the parties, there is ample justification for holding USLIFE liable and bringing it within the scope of our order. [25]

V. THE JENCKS ACT

The ALJ struck the testimony of seven of complaint counsel's witnesses (after they had testified on direct and cross-examination) on the ground that, although reports of interviews of the witnesses conducted by a Commission consumer protection specialist had been turned over to respondents, the interviewer had not kept the rough notes of the interviews after using them to prepare the typed reports. Thus, the notes had not been turned over to respondents pursuant to their request for all witness statements. In striking this testimony, the ALJ was applying what he understood to be the requirements of the Commission's decisions endorsing the principles of the Jencks Act.

The Jencks Act provides that in a criminal case after a witness called by the government has testified, the court shall order the government to:

> produce any statement (as hereinafter defined) of the witness in the possession of the United States which relates to the subject matter as to which the witness has testified. (18 U.S.C. 3500(b))

For purposes of §3500(b), a "statement" is defined to mean:

> (1) a written statement made by said witness and signed or otherwise adopted or approved by him;
>
> (2) a stenographic, mechanical, electrical, or other recording, or a transcription thereof, which is a substantially verbatim recital of an oral statement made by said witness and recorded contemporaneously with the making of such statement; or
>
> (3) a statement, however taken or recorded, or a transcription thereof, if any, made by said witness to a grand jury. (18 U.S.C. 3500(e))

In finding that the seven witnesses made Jencks Act statements, the law judge specifically noted that one witness read and signed the investigator's notes and another reviewed and verified the accuracy of the notes. As to the other witnesses, the ALJ found that either §3500(e)(1) or (e)(2) statements were made. (ID pp. 5–6) Unlike the ALJ, however, we do not believe the issues are quite so clearcut. Indeed, after reviewing the evidence relating to the interviews and the manner in which they were conducted, we have concluded that the ALJ erred in striking the testimony of all seven of the consumer witnesses. [26] Since this testimony is merely cumulative to and corroborative of the documentary evidence and testimony described previously, we have not relied upon it in finding that respondents failed to comply with the applicable provisions of the Truth in Lending Act and Regulation Z.[32] Nevertheless, to provide further guidance on this subject for future Commission proceedings, we believe it is appropriate to review the ALJ's rulings.

At the outset, it is important to reiterate the basis for our consideration of the Jencks Act, in order to dispel some misapprehensions that may exist about the subject.

The Act is by its terms plainly applicable only to criminal prosecutions brought by the United States, 18 U.S.C. 3500(a). It was intended by Congress to narrow the evidentiary ruling of the Supreme Court in *Jencks* v. *United States*, 353 U.S. 657 (1957), to the effect that defendants in federal criminal cases were entitled to inspect reports of FBI interviews of prosecution witnesses who had testified at trial, where the reports touched on the subject of their direct testimony. The legislation confined the reach of that decision by strictly defining the definition of "statement" and prescribing a method for trial judges to separate Jencks from non-Jencks materials. In interpreting the Jencks Act, the Supreme Court has stressed the reasons underlying passage of the legislation, namely Congress' desire to prevent (1) unwarranted disclosure of government files and (2) impeachment of a witness through use of prior statements "which could not fairly be said to be the witness' own rather than the product of the investigator's selections, interpretations, and interpolations." *Palermo* v. *United States*, 360 U.S. 343, 350 (1959). [27]

Although it may once have been thought otherwise,[33] it is now clear that the *Jencks* decision and the principle reflected in the Jencks Act do not reflect any requirement of due process, but are rather only evidentiary matters concerning federal court litigation—a subject over which the Supreme Court and the lower federal courts have special authority, subject to applicable statutes and rules. *See, e.g., United States* v. *Augenblick*, 393 U.S. 348, 356 (1969); *United States* v. *Nobles*, 422 U.S. 225 (1975). As *Nobles* indicates, the Jencks Act is essentially a specific example of a federal trial court's authority to require the production of prior statements of a witness, whether a prosecution witness as in *Jencks*, or a defense witness as in *Nobles*.

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[32] The ALJ, while ultimately striking the testimony of the seven Jencks witnesses, permitted them to testify in full after *voir dire* examination on the Jencks question. (ID p.9) Their testimony fully corroborated the testimony of other witnesses and showed that loan papers with insurance included were prepared in advance of the customer's arrival at USLIFE Credit's office (Tr. 363; 479; 501–03; 827); customers were instructed where to sign for the loan and for insurance (Tr. 368–69; 443; 479; 505; 827); at least one borrower was told insurance was a prerequisite to obtaining the loan (Tr. 551–52); and, despite respondents' practice of going over the loan papers, all the witnesses assumed that insurance was a required part of the bargain. (Tr. 269–71, 275–76; 362–63, 369–70; 443; 479–81; 502–05; 538–39, 545–46; 811, 827)

[33] *See, e.g., Harvey Aluminum Inc.* v. *NLRB*, 335 F.2d 749, 753 (9th Cir. 1964); *Communist Party of the United States* v. *SACB*, 254 F.2d 314, 327–28 (D.C. Cir. 1958).

These principles, however, have no direct application to Commission proceedings. It is well-settled that, subject to applicable statutes and constitutional privileges, independent agencies need not apply any particular evidentiary rules or procedures, and courts are not free to impose on agency proceedings the rules and privileges developed in the exercise of their supervisory power over federal court trials. *F.T.C.* v. *Cement Inst.*, 333 U.S. 683, 705–06 (1948); *Opp Cotton Mills, Inc.* v. *Administrator*, 312 U.S. 126, 155 (1941); *F.C.C.* v. *Pottsville Broadcasting Co.*, 309 U.S. 134, 143 (1940); *Giant Food, Inc.* v. *F.T.C.*, 322 F.2d 977, 984 (D.C. Cir. 1963); *Concrete Materials Corp.* v. *F.T.C.*, 189 F.2d 359, 362 (7th Cir. 1951). *See also Vermont Yankee Nuclear Power Corp.* v. *Natural Resources Defense Council, Inc.*, 46 U.S.L.W. 4301, 4302, 4307 (U.S. April 3, 1978).

The upshot of these decisions, in our view, is that whether or to what extent the principle underlying the Jencks Act and cases construing it should be applied in Commission proceedings is entirely a matter of policy committed to the Commission's discretion. The Commission has previously decided to apply in its proceedings the Jencks Act principle requiring production of certain prior statements by witnesses after they have testified. *See, e.g., Interstate Builders, Inc.*, 69 F.T.C. 1152 (1966); *Ernest Mark High*, 56 F.T.C. 625, 633 (1959).[34] While we find court decisions interpreting the Jencks Act instructive in applying our own Jencks principle, we are, for reasons previously stated, not bound by those decisions.[35] In this context we turn now to a review of Jencks Act cases and the application of our Jencks principle in this case. [28]

The critical threshold issue here is whether a satisfactory showing has been made that the rough interview notes constituted Jencks-type statements to justify striking the testimony of the seven witnesses. Even in a Jencks Act case, the mere failure to produce the notes, without more, does not warrant such a severe sanction. That result is implicit in the Supreme Court's recent decision in *Goldberg* v. *United States*, 425 U.S. 94 (1976), where the Court concluded that the witness' testimony "raised a sufficient showing under the [Jencks] Act" to require the trial judge to conduct a further inquiry. *Id.* at 109. Of course, where the rough notes no longer exist, the inquiry becomes more difficult. If there is evidence that the notes were destroyed in bad faith, that alone may be sufficient cause for striking a witness' testimony. However, as the ALJ pointed out, it appears that the notes were disposed of innocently (ID p. 8), and respondents do not allege otherwise.

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[34] Our prior cases, like this one, have dealt with requests by respondents for production of prior statements by complaint counsel's witnesses. We accordingly have had no occasion to apply the same principle to complaint counsel's request for production of prior statements by respondent's witnesses. *See Nobles, supra.*

[35] Unlike a criminal conviction, a Commission order is typically prospective in effect and cannot result in imprisonment; more pre-trial discovery is available in Commission proceedings than in criminal trials; and the absence of a jury makes inconsistencies between testimony and prior statements somewhat less important as a matter of trial tactics than in a criminal case.

Before examining the facts of this case, a brief review of judicial decisions construing the Jencks Act provides useful guidance to the Commission in making its own determinations. The touchstone in evaluating the status under the Jencks Act of any arguably producible materials is whether they can fairly be said to constitute the witness' own words. *Palermo* v. *United States, supra,* 360 U.S. at 350. That analysis is especially critical in determining whether the witness has adopted or approved the writing made by another under subsection (e)(1) or the interviewer's notes reflect a "substantially verbatim recital of an oral statement" under subsection (e)(2). In either case, the statute contemplates that the product must be that of the witness and not the selections and ruminations of the interviewer.

While adoption may occur when the witness reads the interviewer's notes or has the substance of them read back to him, *Campbell* v. *United States,* 373 U.S. 487, 490–91 (1963); *United States* v. *Annunziato,* 293 F.2d 373, 382 (2d Cir. 1961), to qualify as an (e)(1) statement requires more than casual or selective review. Partial recitals by the interviewer, even verbatim, will not be sufficient to trigger subsection (e)(1). *United States* v. *Smaldone,* 484 F.2d 311, 318 (10th Cir. 1973); *United States* v. *Scaglione,* 446 F.2d 182, 184 (5th Cir. 1971). Nor will general inquiries to the witness concerning the overall veracity of his conversation be sufficient. *Matthews* v. *United States,* 407 F.2d 1371, 1376 (5th Cir. 1969).

Likewise, general give-and-take between the witness and interviewer and periodic requests for clarification will not, standing alone, constitute adoption or approval. As the Supreme Court stated in *Goldberg:* [29]

> Every witness interview will, of course, involve conversation between the [interviewer] and the witness, and the [interviewer] will necessarily inquire of the witness to be certain that he has correctly understood what the witness has said. Such discussions of the general substance of what the witness has said do not constitute adoption or approval of the [interviewer's] notes within § 3500(e)(1), which is satisfied only when the witness has "signed or otherwise adopted or approved" what the [interviewer] has written. This requirement clearly is not met when the [interviewer] does not read back, or the witness does not read, what the [interviewer] has written. (425 U.S. at 110–11, note 19)

In a concurring opinion, Justice Stevens elaborated on the kind of showing that would be necessary to constitute adoption or approval of an interviewer's notes. There must not only be "the kind of factual narrative by the witness that is usable for impeachment" but also "a finding of unambiguous and specific approval by the witness." (*Id.* at 114–15) In describing what constitutes approval, Justice Stevens observed that:

> General testimony that some of the notes taken by the [interviewer] during a lengthy interrogation were read back to the witness, and that the witness sometimes assented to the [interviewer's] version of what he said, would not justify a finding of approval of any particular note. Fairness to the witness demands a much more strict test of approval before he may be confronted with assertedly prior inconsistent statements. (*Id.* at 115)

Fairly rigorous standards have also been applied in determining whether a "substantially verbatim recital" has been made of a witness' comments during the course of an interview. In *Palermo*, the Court looked to legislative history and concluded that "[i]t is clear from the continuous congressional emphasis on 'substantially verbatim recital,' and 'continuous, narrative statements made by the witness recorded verbatim, or nearly so' . . . that the legislation was designed to eliminate the danger of distortion and misrepresentation inherent in a report which merely selects portions, albeit accurately, from a lengthy oral recital." (360 U.S. at 352) This standard has been characterized by the Second Circuit as "very restrictive." *United States* v. *Lamma*, 349 F.2d 338, 340 (2d Cir. 1965) **[30]**

Given this judicial backdrop pertaining to the Jencks Act, we believe that similar criteria should be employed in resolving these issues in Commission proceedings. More specifically, clear and explicit approval by a witness of an interviewer's notes will have to be shown before those notes must be produced as Jencks-type statements in Commission proceedings. Absent such approval, notes must be produced at trial only if they contain the oral narrative of a witness recorded verbatim or substantially verbatim. Within this context, we turn to consideration of the facts of this case.

As we stated earlier, the unavailability of the interview notes makes the task of deciding the Jencks issues somewhat more difficult. Nevertheless, in view of the rather extensive *voir dire* examination of the witnesses and former Commission employee who interviewed them, there is an adequate basis for determining the proper treatment to give this testimony.

The seven witnesses whose testimony was struck provided a variety of answers in describing the note-taking practices of the interviewer, ranging from the recollection of one witness that she signed the notes (Tr. 293) to the statement by another that he didn't sign or look at the notes and couldn't recall whether they were read back to him. (Tr. 522–23) Two other witnesses, Curtin and DeLoatch, testified that they didn't review or sign the notes and were only occasionally asked to repeat their answers. (Tr. 350–52, 354–55; 428, 432) Similarly, in the case of Ms. Knieser, the notes were not read back or signed (Tr. 466), although the witness testified that her responses to the interviewer's questions were written down verbatim. (Tr. 466–67) As for witnesses Garner and Dickerson, the former recalled that he signed the paper containing the questions and answers after glancing over it (Tr. 495–96), but acknowledged that he did not see the questions and it is unclear whether he read the answers (Tr. 495). Mr. Dickerson did not believe he signed the notes but added that the interviewer would go over his responses to see if she had got it correctly and he would make any necessary corrections. (Tr. 795) Finally, the testimony of an eighth witness interviewed by Ms. Turian was not struck by the ALJ (Tr. 310) and respondents did not appeal that ruling. [31]

With the exception of the two witnesses who testified that they signed the notes, the pattern which emerges from the testimony of the other consumer witnesses is largely consistent with the account supplied by the Commission investigator, Ms. Turian. As she described, the interview format involved asking the witnesses a series of predetermined questions. (Tr. 401) Extensive follow-up was unnecessary, since "some of the questions were quite repetitious, and I was getting the same answers more than once. If there was any possibility I thought they did not understand what I was saying, I would say something like, 'in other words,' and I would repeat what they said and ask them if this is correct." (Tr. 402) She further stated that none of the witnesses was asked to review or sign her notes (Tr. 388, 395–96), adding that the only signature she obtained from any witness was in conjunction with the Privacy Act disclosure. (Tr. 398–88)

Respondents, for their part, contend that the testimony shows that the notes were either approved by the witnesses or constituted substantially verbatim recitals of what they said. They argue that the answers elicited here on *voir dire* are at least as compelling as those which the Court in *Goldberg* found to raise sufficient questions to warrant a further inquiry. But the *Goldberg* court did not conclude that a Jencks Act statement had been made; rather it recognized the need for additional hearings on this issue in view of the trial court's erroneous ruling on the "work product" question. (425 U.S. at 108) To the extent there are similarities between this case and *Goldberg*, it seems doubtful whether the testimony in that case, standing alone, would have persuaded the Court that Jencks Act statements were given.[36]

The more extensive evidence available in this case indicates that the majority of the witnesses did not give the kind of specific approval that would justify requiring rough notes to be turned over to respondents. At most, the testimony of Ms. Brooks and possibly witnesses Garner and Knieser reveal either approval or verbatim transcription of a statement. As to the others, we are convinced that the ALJ should have permitted their testimony to stand. [32]

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[36] We note the concurring statement of Justice Stevens, in which he observed that "I do not understand these additional comments to be inconsistent with anything in the court's opinion. . . ." (425 U.S. at 116)

Complaint counsel also advance an alternative basis for not striking the testimony of any of these witnesses, even assuming some of them made Jencks statements, contending that the notes were disposed of in good faith after being incorporated into interview reports. (CAB at 12–16) It is true that some courts have not invoked Jencks Act sanctions where rough notes were destroyed in good faith according to customary procedures and the contents of the notes were preserved in interview reports. *E.g., United States* v. *Pacheo,* 489 F.2d 554, 565–66 (5th Cir. 1974), *cert. denied,* 421 U.S. 909 (1975); *United States* v. *Covello,* 410 F.2d 536, 545 (2d Cir. 1969), *cert. denied,* 396 U.S. 879 (1969); *United States* v. *Lonardo,* 350 F.2d 523, 529 (6th Cir. 1965). *But see, e.g., United States* v. *Carrasco,* 537 F.2d 372 (9th Cir. 1976); *United States* v. *Harrison,* 524 F.2d 421 (D.C. Cir. 1975) (requiring retention of notes). But the record here is inadequate to determine whether the interview reports sufficiently reflect the substance of the notes to serve as an appropriate evidentiary substitute.

We would note, however, that the failure to preserve notes containing Jencks-type statements should not inevitably result in the testimony being struck. Without condoning the withholding of such evidence, we fail to see the need for automatically imposing such a severe sanction irrespective of the circumstances surrounding non-production. Though courts may take a different posture in criminal cases involving the Jencks Act, a less rigid standard is called for in administrative proceedings such as this one. *See* note 35 *supra.* In our view, the administrative law judges may properly exercise discretion in deciding what kind of sanction, if any, is warranted.[37] Nevertheless, given our disposition of this case, we find it unnecessary to disturb the ALJ's choice of remedies here, except insofar as we conclude that no Jencks-type statements were made. [33]

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[37] Such discretion seems particularly appropriate in cases like the one here where the failure to produce materials was not deliberate. Indeed, even under the Jencks Act, district court judges may have more discretion to fashion an appropriate remedy where the government does not consciously elect to withhold otherwise producible documents. As the Sixth Circuit Court of Appeals ruled recently, "subsection (d) [of the Jencks Act, 18 U.S.C. 3500(d)] was not designed to extinguish the normal exercise of judicial discretion by the trial judge where the Act may have been violated by oversight or negligent conduct not amounting to a conscious election." *United States* v. *Pope,* 574 F.2d 320, 325 (6th Cir. 1978).

VI. RELIEF

Complaint counsel have asked the Commission to impose an order similar to the proposed notice order accompanying the complaint. (CAB at 49–51) There is no doubt that the Commission has ample authority to enter an order that not only prohibits the specific practices which formed the basis of the complaint but also fences in respondents as to related conduct. *FTC* v. *Mandel Bros.*, 359 U.S. 385, 392 (1959); *Jacob Siegel Co.* v. *FTC*, 327 U.S. 608, 611 (1946). As long as the remedy is reasonably related to the practices found to be unlawful, the Commission may "frame its order broadly enough to prevent respondents from engaging in similarly illegal practices" in the future. *FTC* v. *Colgate-Palmolive Co.*, 380 U.S. 374, 395 (1965). *See also Nat'l Soc'y of Professional Engineers* v. *United States*, 98 S.Ct. 1355 (1978).

To this end we have incorporated in our order many of the provisions contained in the notice order. Consistent with our finding that respondents violated the law through use of signature indicators and preparation of loan forms with insurance included prior to written authorization, these practices will be proscribed by the order. By requiring respondents to obtain written approval before insurance charges are inserted in the loan agreement, much of the confusion experienced by consumers should be dispelled. Moreover, such a procedure should serve as an inducement for respondents' loan officials to describe the insurance options more fully, since the loan papers cannot be filled out completely until the decision on insurance has been made.[38]

To further ensure that respondents' loan customers will receive meaningful disclosure of their insurance rights, the order requires the disclosures to be provided on a separate document containing no other information. A proposed disclosure statement is attached to the order indicating the type of format which would comply with the terms of our order. We have simplified this form by eliminating, for example, the requirement that [34] separate monthly payment figures be shown for each insurance option. Since monthly payment rates may be set independently of whether insurance is included in the loan contract, the disclosure scheme contemplated by the notice order would be complex and possibly confusing to borrowers. For similar reasons, we have modified paragraph 1 of the order to require disclosure that insurance is voluntary whenever representations are made about insurance coverage (prior to written authorization), rather than in instances where respondents quote monthly payment terms which may include insurance.[39]

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[38] We reject respondents' contention that this requirement will unduly delay the transaction. To be sure, a few computations will have to be done at closing rather than earlier, but that seems essential if consumers are to be afforded a meaningful opportunity to accept or reject insurance. We have, however, eliminated the notice order provision requiring respondents' loan personnel to read the insurance notice to consumers and obtain a written acknowledgement of that action from them. Such a requirement is overly cumbersome and unnecessary for effective relief.

The final order also contains several provisions designed to close off other avenues which might be employed to defeat the borrower's voluntary insurance election. These include prohibitions on (1) discouraging by misrepresentation the declination of insurance, (2) representing that a customer's failure to purchase insurance will delay processing of the loan and (3) failing to disclose the purpose of signatures requested by respondents' loan personnel. In addition, the order specifies that respondents must comply with other applicable requirements of Regulation Z. Such a fencing-in provision is appropriate in view of the fact that the finance charge and annual percentage rate serve as a common link to all disclosure requirements of the regulation.

Finally, we have retained the order provision requiring respondents to maintain records of the percentage of loans made which include insurance. These records are to be kept for each branch office (similar, but informal, records are presently being maintained) on an annual basis and forwarded to the Commission for each of the next five years. Such information will assist the Commission in ascertaining whether the incidence of insurance coverage may warrant further examination. Commission review of respondents' compliance [35] with the order will also be facilitated by requiring submission of a detailed compliance report within 60 days after issuance of the order and annually for five years.[40]

FINAL ORDER

This matter having been heard by the Commission upon the appeals of complaint counsel and respondent USLIFE Corporation from the initial decision, and upon briefs and oral argument in support thereof and in opposition thereto, and the Commission, for the reasons stated in the accompanying opinion, having granted the appeal of complaint counsel and denied the appeal of respondent:

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[39] Our order, of course, does not prevent respondents from discussing insurance on the phone or in person with would-be borrowers. Such discussions are necessary to respond to customer inquiries and facilitate processing of the loan by enabling the lender to ascertain the borrower's needs and the amount of credit that can be extended. However, since insurance charges cannot be included in the loan papers before written authorization is received, there should be a stronger incentive for respondents to provide more accurate oral disclosures to customers in an effort to avoid delay at closing. Thus, the order is fashioned in a manner that enhances the utility of the written disclosures, discourages efforts to circumvent those disclosures through contradictory oral representations, and yet recognizes the practical realities of the lending business.

[40] We have also deleted from the notice order a provision requiring respondents to give all current borrowers an opportunity to cancel their insurance coverage and get a pro rata refund. While such relief, limited as it would be to those borrowers who have not yet paid off their loans, may be appropriate in other instances, we are not persuaded that the circumstances here warrant such action.

It is ordered, That the initial decision and order of the administrative law judge be, and they hereby are, vacated, except to the extent that the initial decision is consistent with the accompanying opinion of the Commission, and the findings of fact and conclusions of law contained in the opinion be, and they hereby are, adopted as the findings and conclusions of the Commission in this matter.

Accordingly, the following cease and desist order is hereby entered. [2]

ORDER

It is ordered, That respondents USLIFE Credit Corporation, a corporation, and USLIFE Corporation, a corporation, their successors and assigns, and their officers, and respondents' agents, representatives and employees, directly or through any corporation, subsidiary, division or other device, in connection with any extension of consumer credit, as "consumer credit" is defined in Regulation Z (12 C.F.R. 226) of the Truth in Lending Act (Pub. Law 90-321, 15 U.S.C. 1601, *et. seq.*) do forthwith cease and desist from:

1. Failing, when the charges for credit life insurance and/or credit accident and health (disability) insurance are not included in the finance charge, to quote the costs of any credit insurance coverage or to refer in any way to the availability of such coverage, either orally or in writing, without clearly disclosing that:

(a) credit life insurance and/or credit accident and health (disability) insurance are optional; and

(b) the consumer's choice regarding insurance coverage will not be considered in respondents' decision to approve credit for such consumer,

Respondent's obligation under this paragraph shall end concurrently with the customer's execution of the separate, voluntary insurance election form required by paragraph 2.

2. Failing, when the charges for credit life insurance and/or credit accident and health (disability) insurance are not included in the finance charge:

(a) to present to the borrower as the first document at the time of closing, a separate, voluntary insurance election form which sets forth clearly and conspicuously the following information:

(i) the purchase of credit insurance is not required by USLIFE Credit Corporation [or other business extending consumer credit] in connection with this loan [or other extension of consumer credit];

(ii) the borrower's decision with regard to the insurance available through respondents is not considered in granting the credit; [3]

(iii) the amount of the total premium for credit life insurance and/or the total premium for credit accident and health (disability) insurance;

(iv) the borrower authorizes respondents on behalf of the borrower to pay the insurance premiums to the insurance company for such credit insurance as has been chosen;

(v) each option available to the borrower; and

(vi) a signature and date line for each option set forth in (v) above for the consumer to indicate his/her election.

(b) Failing to make the disclosures required by subparagraph (a) on a separate document which contains no other printed or written material. The disclosures required by subparagraphs (i), (ii), and (iii) shall not be smaller than 12 point type. A form substantially in conformance with Attachment A herein will be considered as in compliance with the provisions of subparagraphs (a) and (b). Respondents shall maintain the original form for two years following its execution and provide the customer with an executed copy thereof.

(c) Failing to leave the Truth in Lending disclosure statement blank as to the cost of credit life insurance and/or credit accident and health (disability) insurance and all other information or amounts which are affected by the election or declination of insurance until the borrower has signed the written disclosure required by subparagraph (a).

(d) Making any marks or otherwise instructing a consumer where to sign or date the separate voluntary insurance election form required by subparagraph (a) in advance of the consumer's free and independent choice for such insurance.

(e) Misrepresenting, orally or otherwise, directly or by implication, that credit life and/or credit accident and health (disability) insurance are required as a condition of obtaining credit from respondents. [4]

(f) Discouraging, by misrepresentation, oral or otherwise, directly or by implication, the declination of credit life and/or credit accident and health (disability) insurance.

(g) Representing, orally or otherwise, directly or indirectly, that the consumer's failure to elect credit insurance will result in delay in processing the loan or distributing the proceeds.

3. Failing to tell every customer the purpose(s) of each signature requested by respondents on any document directly related to the consummation of the credit transaction.

4. Failing to compute and disclose accurately the finance charge, as required by Sections 226.4(a)(5) and 226.8(d) of Regulation Z.

5. Failing to compute and disclose accurately the annual percent-

age rate to the nearest quarter of one percent as required by Sections 226.5(b) and 226.8(b) of Regulation Z.

6. Failing, in any consumer loan transaction or advertisement, to make all disclosures, determined in accordance with Sections 226.4 and 226.5 of Regulation Z, in the manner, form and amount required by Sections 226.6, 226.8, 226.9, and 226.10 of Regulation Z.

It is further ordered:

(a) That respondents maintain records on an annual basis for each branch office of the penetration rate of:

(1) credit life insurance, stating the rate separately for both direct loans and installment sales contracts; and

(2) credit accident and health (disability) insurance, stating the rate separately for both direct loans and installment sales contracts. Such records shall be submitted to the Commission each year for a period of five years following the effective date of this order and thereafter upon request.

For purposes of this subparagraph, the term "penetration rate" means the percentage of all contracts eligible for credit insurance on which charges for such insurance are made. In reporting penetration rates the respondents must state the total number and dollar amount of loans and installment contracts entered into which were eligible for credit insurance, stated separately for credit life and credit accident and health (disability) insurance. [5]

(b) That respondents deliver a copy of this order to cease and desist to all present and future personnel of respondents at their home and regional offices and in each of their subsidiary loan offices which are engaged in the extension of consumer loans, and that respondents secure a signed statement acknowledging receipt of said copy of this order from each such person.

(c) That respondents notify the Commission within thirty (30) days of any change in the corporate respondents which may affect compliance obligations with regard to the extension of consumer loans arising out of this order, such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporations with regard to the extension of consumer loans which may affect compliance obligations arising out of this order.

(d) Respondents herein shall, within sixty (60) days after service of this order, and annually for five (5) years thereafter, file with the Commission a written report setting forth in detail the manner and form of their compliance with this order. The expiration of the obligation to file such reports shall not affect any other obligation arising under this order.

Commissioner Pitofsky did not participate.

ATTACHMENT A

VOLUNTARY INSURANCE ELECTION

YOU ARE *NOT* REQUIRED TO PURCHASE CREDIT LIFE OR DISABILITY INSURANCE TO OBTAIN THIS LOAN. YOUR DECISION ABOUT INSURANCE DOES *NOT* AFFECT THE AMOUNT OF CREDIT APPROVED FOR YOU.

Insurance Premiums (if desired)

Credit Life $________________

Credit Disability $________________
(accident & health)

Combined Life and Disability $________________

YOUR CHOICES ARE SHOWN BELOW. IF YOU ELECT TO PURCHASE CREDIT INSURANCE, THE PREMIUM(S) WILL BE PAID FROM THE PROCEEDS OF THE LOAN ON YOUR BEHALF BY THE LENDER. I/WE HAVE CHOSEN THE FOLLOWING OPTION:

I/We Do *NOT* Want Credit Insurance	**I/We Want Credit Life Only**	**I/We Want Credit Disability Only**	**I/We Want Credit Life & Disability**
________________	________________	________________	________________
(Borrower)	**(Borrower)**	**(Borrower)**	**(Borrower)**
________________	________________	________________	________________
(Co-Signer)	**(Co-Signer)**	**(Co-Signer)**	**(Co-Signer)**
________________	________________	________________	________________
Date	**Date**	**Date**	**Date**

IN THE MATTER OF

CAPAX, INC. FORMERLY CONTINENTAL CREDIT CORPORATION, INC., ET AL.

Docket 9058. Complaint, Sept. 30, 1975—Final Order, May 25, 1978

This order, among other things, requires a Willingboro, N.J. debt collection company to cease misrepresenting its status, activities or actions; the affect of nonpayment on credit ratings; and the imminency of legal action. The firm is further prohibited from using, or placing in the hands of others, forms and materials which simulate telegrams, or which otherwise misrepresent the nature, urgency and import of communication, to induce payment of delinquent debts.

Appearances

For the Commission: *Alan D. Reffkin, Carthon E. Aldhizer* and *John F. LeFevre.*

For the respondents: *Robert Field Stockton, David Lyle Segal* and *Steven A. Segal, Segal & Stockton,* Philadelphia, Pa. for Capax, Inc., Continental Credit Corporation, Inc., Joseph V. DeFelice and Arnold Goodman and *Barbara Van Horn Colsey,* Delanco, N.J. for Norman Bricker.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Capax, Inc., a corporation, formerly Continental Credit Corporation, Inc., a corporation, and Joseph V. DeFelice and Arnold Goodman, individually and as officers of said corporation, and Norman Bricker, individually and as a former officer of said corporation, hereinafter sometimes referred to as respondents, have violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent Capax, Inc., formerly Continental Credit Corporation, Inc., is a corporation organized, existing and doing business under and by virtue of the laws of the State of New Jersey, with its principal office and place of business located at Route 130 and Beverly-Rancocas Road, Willingboro, New Jersey.

Respondents Joseph V. DeFelice and Arnold Goodman are individuals and are officers of the corporate respondent. They formulate, direct and control the acts and practices of the corporate respondent, including the acts and practices hereinafter set forth. Their address is the same as that of the corporate respondent. [2]

Norman Bricker is an individual and, up to March 1975, was an officer of corporate respondent. Until his resignation, he formulated, directed and controlled the acts and practices of the corporate respondent, including the acts and practices hereinafter set forth. His address is 504 Route 130 N., Cinnaminson, New Jersey and P.O. Box 123, Delanco, New Jersey.

PAR. 2. Respondents are now, and for some time in the past have been, engaged in advertising, offering for sale and sale of a service to assist in the collection of alleged delinquent debts. This service consists of preparation by respondents of a series of form notices and letters to be mailed to alleged delinquent debtors at regular intervals. Two styles of forms are or have been used in the series: (1) that which is titled LETEGRAM; (2) that which bears the letterhead styled Continental Credit Corporation . . . . . Credit Control and Collection.

PAR. 3. In the course and conduct of their business, respondents are now, and for some time in the past have been, engaged in sending to and receiving from persons, firms, and corporations located in various States of the United States, by means of the United States mail, letters, notices, forms and other material for use in the collection of alleged delinquent debts. Respondents maintain, and at all times mentioned herein have maintained, a substantial course of trade in said business in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act.

PAR. 4. In the course and conduct of their business, and for the purpose of inducing the payment of alleged delinquent debts, the respondents have mailed or caused to be mailed to alleged delinquent debtors various printed forms, letters and other printed material.

Typical and illustrative, but not necessarily all inclusive of said forms and material, are the following:

(1) a window envelope on which a return address is printed, with no name. The word LETEGRAM is printed in large red type in one location and in large white type in two locations on the face of and the rear side of the envelope.

(2) a printed form styled LETEGRAM, designed to be inserted in the envelope described in subparagraph 1 of this paragraph. [3]

PAR. 5. By and through the use of the envelopes and forms described in subparagraphs 1 and 2 of Paragraph Four, respondents have represented, directly or by implication, that they are telegraphic or other similarly urgent communications.

PAR. 6. In truth and in fact, the envelopes and forms referred to in Paragraphs Four and Five are not telegraphic or other similarly urgent communications. Rather, they are printed form letters, mailed to alleged delinquent debtors, which forms by their overall appearance, styling, printing and format simulate telegraphic or other similarly urgent communications. By virtue of said simulation, these envelopes and forms mislead the recipient as to their nature, import, purpose and urgency.

Therefore, the use by respondents of said envelopes and forms as set forth in Paragraph Four was and is false, misleading and deceptive.

PAR. 7. In the course and conduct of their business, and for the purpose of inducing the payment of alleged delinquent debts, respondents have mailed, or caused to be mailed to alleged delinquent debtors various printed forms, letters and other printed material containing certain statements in either the English or Spanish language.

Among and typical, but not all inclusive, of such statements are the following:

CONTINENTAL CREDIT CORP. . . . .CREDIT CONTROL AND COLLECTION

* * * * * * *

COLLECTION DEPARTMENT

* * * * * * *

YOUR DELINQUENT ACCOUNT WITH [CREDITOR'S NAME] HAS BEEN REFERRED TO CONTINENTAL CREDIT CORPORATION FOR ACTION. . .YOUR CREDITOR HAS REQUESTED THAT YOU BE GIVEN SEVEN DAYS TO SETTLE THIS ACCOUNT. . .

PAID IN FULL WITHIN SEVEN DAYS, THIS ACCOUNT WILL NOT BE SHOWN ON OUR CREDIT RECORDS. . .

* * * * * * *

UP TO NOW YOUR CREDIT STANDING WITH [CREDITOR'S NAME] HAS BEEN SATISFACTORY. CREDIT IS A PRIVILEGE, NOT A RIGHT. [4] IT IS ALMOST IMPOSSIBLE TO REPLACE. LIKE MOST OTHER PRIVILEGES, YOU ONLY MISS IT WHEN YOU NEED IT. . .LET'S NOT PERMIT THE WORST TO HAPPEN.

* * * * * * *

STRONG ACTION IS OFTEN NECESSARY TO COLLECT AN ACCOUNT. . . IF YOU CONTINUE TO IGNORE REQUESTS FOR A FRIENDLY DISPOSITION OF THIS CLAIM YOU MUST ACCEPT THE RESPONSIBILITY FOR FUTURE ACTION.

* * * * * * *

. . .IT IS THE INTENTION OF OUR CLIENT TO EXHAUST EVERY LEGAL

AVENUE AT THEIR DISPOSAL IN ORDER TO COLLECT THIS CLAIM. IF YOU PERSIST IN NOT FOLLOWING THROUGH YOUR OBLIGATION, WE WILL HAVE TO RECOMMEND A MORE DRASTIC ACTION THAT IN THE END WILL BE MUCH MORE COSTLY TO YOU. IF THIS IS YOUR INTENTION I WOULD RECOMMEND THAT YOU CONTACT YOUR ATTORNEY SO HE MAY ADVISE YOU ON THE LEGAL RAMIFICATIONS YOU MAY BE EXPOSED TO.

* * * * * * *

IMPERATIVE THAT SATISFACTORY ARRANGEMENTS BE MADE TO AVOID FURTHER ACTION AVAILABLE TO CLAIMANT UNDER PROVISIONS OF STATE STATUTES. . .IF SETTLEMENT IS NOT MADE WITHIN 48 HOURS UPON RECEIPT OF THIS LETEGRAM, WE SUGGEST YOU CONTACT YOUR ATTORNEY TO DETERMINE YOUR LEGAL LIABILITY.

* * * * * * *

YOUR REFUSAL OR NEGLECT TO SATISFY THE ABOVE LIABILITY COMPELS US TO NOTIFY YOU TO PRESENT ANY DEFENSE AGAINST THE VALIDITY OF THIS CLAIM ON FILE. YOU MAY PROTEST SAID CLAIM OR LIST PROPERTY WHICH YOU FEEL MAY BE EXEMPT, IF [CREDITOR'S NAME] OBTAINS A JUDGMENT. . .

* * * * * * *

[CREDITOR'S NAME] HAS TURNED OVER TO US THEIR CLAIM AGAINST YOU. . .

* * * * * * *

WE ARE WRITING THIS LETTER TO INFORM YOU OF THE SERIOUSNESS OF YOUR DELINQUENCY AND THE FACT THAT, SHOULD IT CONTINUE ALL POSSIBLE LEGAL MEANS WILL BE TAKEN TO COLLECT IT. [5]

* * * * * * *

. . .CONTINENTAL CREDIT CORPORATION CAN TAKE NO OTHER POSITION BUT TO RECOMMEND A STRONGER COURSE OF ACTION TO OUR CLIENT. . .IF THIS IS DONE THERE MAY BE ADDITIONAL COSTS TO YOU AND YOUR CREDIT STANDING MAY SUFFER.

* * * * * * *

[CREDITOR'S NAME] IS ABLY REPRESENTED BY LEGAL COUNSEL WHO, IF CALLED UPON WILL PURSUE THE APPROPRIATE LEGAL MEANS TO LIQUIDATE THIS OUTSTANDING DEBT. . .SHOULD JUDGMENT BE TAKEN AGAINST YOU, THE COURT MAY CHARGE YOU FOR LEGAL COSTS AND FEES.

YOU ARE HEREBY REQUESTED TO APPEAR BETWEEN THE HOURS OF 10 AM AND 4 PM AT THE CLAIMANTS OFFICE AS SET OUT ABOVE WITHIN THREE DAYS AFTER DELIVERY HEREOF TO PROTEST LIABILITY OF CLAIM ON FILE. . .FAILURE TO COMPLY AND APPEAR EITHER IN PERSON OR HAVE LEGAL REPRESENTATIVE ATTEND ON YOUR BEHALF MAY RESULT IN START OF LEGAL ACTION.

PAR. 8. By and through the use of the aforesaid statements, and others of similar import and meaning not expressly set forth herein, including the use of the word "collection" in the corporate letterhead, letters, and envelopes, respondents have represented, directly or by implication, that:

1. Delinquent debtors' accounts have been referred to respondents as an independent debt collection agency which will engage in typical debt collection activities such as making personal demands for payment and/or filing suit.
2. Unless payment is received, steps will be taken to initiate legal action against the alleged debtor.
3. Unless payment is received, respondents will take action to adversely affect the debtor's credit record with a consumer reporting agency.
4. Unless payment is received within the time specified by respondents, immediate action will be taken to collect the debt, such as the filing of suit.

PAR. 9. In truth and in fact:

1. Delinquent debtors' accounts had not been referred to respondents as an independent debt collection [6] agency which would engage in typical debt collection activities such as making personal demands for payment and/or filing suit. In fact, no such action was taken during the course of respondents' form letter service.
2. If payment was not received, steps were not taken to initiate legal action against the alleged debtor; in fact, no action was taken during the form letter series except to send additional form letters to the alleged debtor or to return the uncollected account to the creditor.
3. If payment was not received, respondents took no action to adversely affect the debtor's credit record with a consumer reporting agency.
4. If payment was not received during the time specified by respondents, immediate action was not taken to collect the debt; in fact, the only subsequent action was either the sending of additional form letters to the alleged debtor or returning the uncollected account to the creditor.

Therefore, the statements and representations set forth in Paragraphs Seven and Eight were and are false, misleading and deceptive.

PAR. 10. In the course and conduct of their business, and at all times mentioned herein, respondents have been, and are now, in substantial competition, in commerce, with corporations, firms and individuals engaged in providing services of the same general kind and nature as those provided by respondents.

PAR. 11. The use by respondents of the envelopes and forms, as set forth in Paragraph Four hereof, has had the tendency and capacity to mislead and deceive members of the public into the erroneous and mistaken belief that the said envelopes and forms are telegraphic or other similarly urgent communications. Furthermore, the use by respondents of the aforesaid false, misleading and deceptive statements, representations and practices has had the tendency and capacity to mislead members of the public into the erroneous and mistaken belief that said statements and representations were and are true and to induce the payment of substantial sums of money by reason of said erroneous and mistaken belief. [7]

PAR. 12. The aforesaid acts and practices of respondents, as herein alleged, were and are all to the prejudice and injury of the public and of respondents' competitors and constituted, and now constitute, unfair methods of competition and unfair and deceptive acts and practices in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act.

INITIAL DECISION BY PAUL R. TEETOR, ADMINISTRATIVE LAW JUDGE

APRIL 22, 1977

[2] I

HISTORY OF THE CASE

A. COMPLAINT

On September 30, 1975, this Commission issued its complaint and notice of proposed order against a New Jersey-based commercial debt dunner, Capax, Inc., (hereafter "Capax"), and certain allegedly dominant figures therein. It recited reason to believe that respondents had been using unfair and deceptive acts and practices in their debt dunning business, in violation of Section 5 of the Federal Trade Commission Act, and reciting further that a proceeding with respect to such possible violation appeared to be in the public interest. There followed the usual allegations concerning the respondents' identities, and responsibilities, engagement in interstate commerce, etc. (Pars. 1–3)

The gist of the complaint is that for a flat fee Capax has been sending the debtors of its clients various series of standardized dunning letters which have tended to deceive these debtors into paying their bills. By using the word "collection" in Capax' corporate letterhead, letters and envelopes and by making or implying various statements in its dunning letters (many illustrated in Complaint Par. 7)

Capax' statements allegedly tended to deceive these delinquent debtors in four ways:

(1) By saying or implying that such debtors were being pursued by an "independent debt collection agency"[1] which would "engage in typical debt collection activities such as making personal demands for payment and/or filing suit." In fact, the complaint alleges no such action was taken while the dunning series took its course. (Complaint Pars. 8.1 and 9.1). [3]

(2) By saying or implying that unless payment were received, steps would be taken [by whom is not specified] to "initiate legal action" against the debtor. In fact, the complaint alleges, the only action taken was to send more dunning letters or return the uncollected account to the creditor. (Complaint Pars. 8.2 and 9.2.)

(3) By saying or implying that unless payment were received, respondents would take action to "adversely affect the debtor's credit record" with a "consumer reporting agency." In fact, the complaint alleges, no such action was ever taken by respondents. (Complaint Pars. 8.3 and 9.3.)

(4) By saying or implying that unless payment were received "within the time specified by respondents" "immediate action" to collect the debt, such as filing suit, would be taken. In fact, the complaint alleges, the only action taken was to send more dunning letters or return the uncollected account to the creditor.

The complaint also charges that Capax sometimes uses for its dunning letters and/or envelopes a so-called LETEGRAM, which in overall appearance, styling, printing and format "simulates telegraphic or other similarly urgent communications," so that "by said simulation" recipients are deceived and misled as to the "nature, import, purpose and urgency" of such dunning messages. (Complaint, Par. 4, 5, 6.)

The texts of Capax' dunning letters collected in Complaint Par. 7 and making the above alleged misrepresentations, whether in LETEGRAM or other form, are claimed to have a tendency and capacity to make debtors pay substantial sums they might not otherwise pay, thus constituting such dunning letters unfair and deceptive commercial practices,[2] to the prejudice and injury of the public. (Pars. 11 and 12.) [4]

The notice-order would make respondents cease and desist from:

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[1] Complaint counsel would define an "independent debt collection agency" as "one which takes an *assignment* of a claim of debt for collection on a *commission basis* and engages in such debt collection activities as making personal demands for payment and/or *filing suit*" [CX 60(e)] (emphasis added) but respondents strenuously denied a request to admit this [CX 61(h)]. The complaint itself attempts no definition.

[2] The complaint also charges (in Par. 10 and again in Par. 12) that the same practices constitute unfair methods of competition, presumably with other dunners, but this aspect of the complaint was never pursued and we disregard it here.

(1) misrepresenting its dunning letters as telegrams;

(2) misrepresenting "the nature, import, purpose or urgency" of any communication, except in the case of a truthful and non-conspicuous reference to or implication of urgency;

(3) misrepresenting itself to debtors as an "independent debt collection agency" engaged in "typical debt collection activities;" misrepresenting that steps "may or will" be taken to initiate legal action, unless payment is received; misrepresentating that respondents will take action to adversely affect the debtor's credit record with a consumer reporting agency or any third party or "otherwise misrepresent the impact or effect of non-payment upon the debtor's credit record "unless payment be received; misrepresenting that immediate collection action such as filing suit will be taken unless payment be received within the time specified by respondents, or "otherwise misrepresent the imminency of any action that respondents "may or will" take *provided, however,* that factual correctness of a misrepresentation shall be a defense to any charge of violating any of the prohibitions of (3);

(4) failing to state clearly and conspicuously in any dunning letter that:

> ***This communication is a reminder of creditor's claim. Capax, Inc. does not take any legal or other action against the debtor during this letter writing series.***[3] **(emphasis added) [5]**

(5) undermining the affirmative disclosure provision of (4) above by including any negative or inconsistent statement in dunning letters;

(6) placing in others' hands the means to make any of the representations forbidden in (3) above or to defeat (4) or (5) above;

The proposed order also contains routine provisions for circulation of the order; notification of structural corporate changes by respondent; and notification of changes in individual respondents' employment or business affiliations.

B. JOINT ANSWER

The joint answer of Capax and Messrs. Goodman and DeFelice (hereafter "the joint answer") was filed on 12/18/75, pursuant to two extensions of time beyond the normal 30 days within which to answer. The joint answer admitted most formal matters pleaded in the complaint but took absolute or qualified issue with most of the allegations of substance, including those regarding the LETEGRAM

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[3] A long and complex proposed proviso would avoid operation of the second sentence of the above disclaimer where suit or other action actually follows threat, in certain circumstances.

(Pars. 4, 5, 6) and the dunning misrepresentations alleged in Pars. 8 and 9, although we note that it admitted the "literal truth" of Par. 7's illustrative excerpts from Capax' dunning letters.

In specific response to the four key charges of Complaint Pars. 8 and 9 and the LETEGRAM allegations of Pars. 4–6, the joint answer elaborated respondents' position as follows.

(1) *"Collection Agency" Image* (re Complaint Pars. 8.1 and 9.1)

It is admitted that Capax is an "independent debt collection agency" in the sense that it is "neither owned nor controlled by any of [its] clients" (which is not, however, the way complaint counsel use the term[4]). It further pleads that it now engages in such "typical debt collection activities" as "making personal demands for payment and/or filing suit." It is only said to [6] have done so, however, since about 5/1/75, when, in response to the Commission's proposed complaint (received 12/31/74), Capax is alleged to have started a "hard core" "collection department" which now makes phone calls and arranges with attorneys to commence litigation in the absence of contrary instructions from the creditor, in order for Capax to become a "full service" collection agency.

(2) *Threats of Suit* (re Complaint Pars. 8.2 and 9.2)

Capax denies representing to delinquent debtors that legal action "will" be taken but pleads that in fact respondents do take steps to see that legal action is initiated, if the debt remains unsatisfied, in the absence of contrary instructions from the creditor. [The actual taking of such steps, however, apparently refers only to the period since about 5/1/75, as explained in the previous paragraph.]

(3) *Threats to Credit Standing* (re Complaint Pars. 8.3 and 9.3)

The joint answer flatly denies ever having referred to any "consumer reporting agency," directly or by implication, in any of its dunning activities, although pleading that it has sometimes mentioned the effect of non-payment on debtors' credit standing" with their own creditor(s)."

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[4] See fn. at p. 2 above.

(4) *Threats to Enforce Immediate Action* (re Complaint Pars. 8.4 and 9.4)

The joint answer denies that respondents have ever specified periods within which suit "will" be filed.

(5) *Alleged Deceptive Appearance* (Complaint Pars. 4–6)

The joint answer admits mailing various printed materials to delinquent debtors to induce payment of their debts but describes the type of envelope and form labeled LETEGRAM as magenta and gray rather than red and white (the complaint's description). [7] (Par. 4 and Exhibits D–3 and D–4 to joint answer.).[5] It denies any representation, express or implied, that LETEGRAMS are "telegraphic communications" or are "of an urgency on a par with that of a telegram" but pleads that such envelopes and forms "are used to imply urgency" (and, indeed, sometimes say so, as in Exhibit D–4 to the joint answer). The word "urgency" is said to refer to the creditor's need to maintain his working capital and retain his debtor's patronage; the debtor's need to keep up his standing with the creditor; the country's interest in promoting interstate commerce; and the interest of all consumers who pay their bills in not being saddled with the inevitable expense to them when other consumers fail to pay for what they get. (Par. 5). Accordingly the joint answer denies that recipients of Capax' LETEGRAMS are misled as to their "nature, import, purpose and urgency" (Par. 6).

(6) *Deceptiveness and Unfairness* (Complaint Pars. 11–12)

The joint answer flatly denies having taken any action or made any statement with a tendency or capacity to deceive or mislead anyone and asserts that any monies paid by debtors whom Capax may have dunned were paid "because a valid debt was overdue to the named creditor by the recipient of the letter, phone call or legal action." (Par. 11) Finally, it denies: (1) *engagement* in the alleged deceptive acts and practices; (2) *prejudice or injury* resulting from such acts and practices; and (3) *deceptiveness or unfairness* of such acts and practices under Section 5 of the Federal Trade Commission Act. (Par. 12)

C. RESPONDENT BRICKER'S ANSWER

On 12/23/75 individual respondent Norman Bricker filed his own answer to the complaint pursuant to extensions of time granted therefor. Its allegations generally follow those of the joint answer, with minor differences, except for two matters. He consistently denied knowledge of Capax' affairs after 3/18/75, when [8] he left the company, and even as to the period prior thereto he denied that, as charged in Complaint Par. 1, he "formulated, directed and controlled the acts and practices set forth in the complaint." (Bricker's Answer, Par. 1).

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[5] In Par. 6 of the joint answer respondents allege, with details, that the LETEGRAM was "specifically designed so as not to be confused with a telegram."

D. PRE-TRIAL PROCEEDINGS

(1) *Administrative Law Judge*

This matter was originally assigned on 9/30/75 to Hon. Thomas F. Howder, Administrative Law Judge, for hearing and decision. In view, however, of Judge Howder's opinion that he was disqualified to sit in this matter, it was reassigned on 10/31/75 to Paul R. Teetor, another administrative law judge, who has taken all testimony, received all evidence and performed all other duties provided by law for the hearing and decision of such a matter.

(2) *Service and Appearance of Parties*

Service of the complaint was made on respondents by delivery via registered mail on the following dates:

Capax, Inc.	10/31/75
Joseph DeFelice	10/31/75
Arnold Goodman	10/31/75
Norman Bricker	11/13/75[6]

By letter dated 11/11/75, Robert Field Stockton, Esq., renewed an earlier entry of appearance during pre-complaint proceedings by the firm of Segal & Stockton of Philadelphia, Pennsylvania for respondents Capax, Inc., Joseph V. DeFelice and Arnold Goodman in this matter. Other members of that firm who have since appeared with Mr. Stockton are David Lyle Segal, Esq. and Steven A. Segal, Esq. At the same time he (Stockton) withdrew his earlier appearance for respondent Norman Bricker, who thereafter, on 11/21/75 appeared by a different attorney, Barbara Van Horn Colsey, Esq., of Delanco, New Jersey. [9]

Counsel who have appeared in support of the complaint in this matter are Alan D. Reffkin, Esq., Carthon E. Aldhizer, Esq. and John

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[6] Secondary service was made on respondent Bricker because the original service may have been defective.

F. LeFevre, Esq. all of the Commission's Bureau of Consumer Protection.

(3) *Prehearing Conference (12/23/75)*

Following the filing of respondents' Answers on 12/18/75 as noted above, a prehearing conference was convened in Washington, D.C. on 12/23/75 for opening statements by counsel to familiarize the administrative law judge with the parties' positions and for scheduling of further prehearing procedures, both of which were accomplished. (For details of discovery schedule see Prehearing Order No. 1, 12/24/75.)

At the conference a motion which had been filed on 12/5/75 by respondents to sever the trial of respondent Norman Bricker from the trial of all other respondents was denied from the bench on the authority of Rule 20(b) of the Federal Rules of Civil Procedure for failure to show likelihood of sufficient delay or prejudice to justify severance.

(4) *Pre-trial Briefs*

Pre-trial briefs for early sharpening of the issues were filed by complaint counsel on 1/9/76, by respondent Bricker on 2/2/76 and by other respondents on 2/3/76.

(5) *Motion for Protective Order*

On 3/15/76 respondents Capax, DeFelice and Goodman moved for a "protective order" appointing an "independent canvassing agent" to determine in advance whether any debtor that complaint counsel wanted to interview really remembered anything about Capax and its activities before being interviewed by counsel. Complaint counsel filed an opposition on 3/17/76 and the motion was denied on 3/22/76.

(6) *Discovery and Turnover Schedule*

By May of 1976 the original schedule for pretrial preparation had fallen badly behind without fault on [10] anyone's part, largely because of a massive canvass by complaint counsel of some two thousand debtors whom Capax had dunned. The schedule for discovery of evidence and turnover of each party's case was accordingly revised in Prehearing Order No. 3 (5/25/76) with the aim of having the case ready for trial by Fall and trial was tentatively set to begin 9/13/76.

(7) *Complaint Counsel's Requests for Admissions*

Complaint counsel on 6/11/76, at the time of turning over their case to respondents, filed requests for both factual and documentary admissions by Capax which requests were answered on 7/13/76 by respondents Capax, Inc., DeFelice and Goodman, who made many of the requested admissions but qualified some and denied others. See CX 60(a)-(r) and CX 61(a)-(i). The substantive admissions were later reviewed and approved individually (with only minor modifications) in open court. See Tr. 225–245. Documentary admissions were generally referred to when the relevant document was offered into evidence. Respondent Bricker's counsel received the same requests, although without illustrative attachments. (Tr. 92.) Although absent when these admissions were reviewed and generally approved in open court on 10/27/76, she assured the court that she felt her client (Bricker) was adequately represented by Capax' attorneys, Messrs. Stockton and Segal, for that session. (Tr. 301.)

(8) *Re-scheduling of Hearings*

On 9/10/76 the hearing originally scheduled for 9/13/76 was rescheduled to begin 10/26/76, in order to extend respondents' time to turnover their case to complaint counsel from 8/20/76 to 9/28/76 and a preclusion order was entered with respect to any such evidence not in complaint counsel's hands by the 28th.

(9) *Respondents' Requests for Admissions*

On 10/4/76 respondents Capax, Inc., DeFelice and Goodman, with the turnover of their case, filed requests for both factual and documentary admissions, which [11] requests were answered on 10/13/76 by complaint counsel, who on 10/13/76 made some admissions but objected to many others. Their answer was never made an exhibit during the later hearing but is on file with the Secretary.

(10) *Motion to Change Venue*

Also on 10/4/76 respondents Capax, Inc., DeFelice and Goodman[7] filed a motion for a "change of venue" to move the up-coming hearing from Washington, D.C. to Philadelphia, Penn. on the ground that that would be a more convenient location for everyone but complaint counsel. Opposition by complaint counsel was filed on 10/8/76 and on 10/15/76 the motion was denied.

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[7] On 10/12/76 Ms. Colsey filed a "supporting affidavit" for respondent Bricker.

(11) *Motion for Appointment of Expert Witnesses*

Also on 10/4/76 respondents Capax, Inc., DeFelice and Goodman[8] filed a motion for appointment of expert witnesses for respondents at Commission expense (estimated at about $5000) and asked incidentally for *in camera* treatment of this and all other pending motions. On 10/6/76 the administrative law judge denied the request for *in camera* treatment, but certified the motion for appointment of expert witnesses to the Commission without recommendation, as a matter of administrative discretion. The Commission did not act on this certification until after the hearings had been held. At the close of the hearings on 11/4/76, respondents voluntarily withdrew this motion, despite an offer by the administrative law judge to hold the record open in case the Commission should decide the motion in favor of said respondents (Tr. 1009, 1014, 1020). On 11/5/76 the Commission was formally notified of said respondents' withdrawal of their motion and on 1/24/77 the Commission, "being satisfied that respondents voluntarily relinquished their request for appointment of expert witnesses," denied the motion as "moot." [12]

(12) *Motion To Disqualify Administrative Law Judge*

Also on 10/4/76 respondents Capax, Inc., DeFelice and Goodman filed a motion asking the administrative law judge to disqualify himself from presiding in this case, on authority of 16 C.F.R. 4.7, on the ground that in July complaint counsel had written one letter to the judge (with carbon copy to opposing counsel) alleging "intimidation" of complaint counsel's witnesses by respondents counsel and in September had written another letter to the Judge (again with carbon copy to respondents' counsel) charging "intimidation and threats to witnesses" in an anonymous phone call which complaint counsel suspected must be attributed to "a representative of Capax." Complaint counsel's opposition was filed on 10/8/76. On 10/14/76 the administrative law judge, having elected not to disqualify himself within 10 days, certified the motion to the Commission as required by Rule 3.42(g)(2), explaining that the communications in question were not *ex parte* and the judge's mind had not been poisoned in any way. On 10/20/76 the Commission affirmed the judge's decision not to disqualify himself, holding that the sending of carbon copies prevented the communications from being *ex parte* and that no showing had been made that the judge's ability to conduct a fair trial had been prejudiced in any way.

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[8] On 10/12/76 Ms. Colsey filed a "supporting affidavit" for respondent Bricker.

E. TRIAL

(1) *Witnesses*

Evidentiary hearings in this matter were held in Room 332 of the Federal Trade Commission Building in Washington, D.C. on October 26, 27, 28 and 29 and in Room 7314 of the Old Star Building in Washington, D.C. on November 3 and 4, 1976. Witnesses called by complaint counsel, the dates of their testimony and references to the relevant transcript pages are as follows:

Date	*Transcript Start*	*Name*	*Home Address*
Witnesses called by complaint counsel were as follows:			
10/26/76	p. 116	Peggy Jean Thom	Mill Lane Columbus, N.J.
	p. 146	Charlene Nield	2745 29th St., N.W. Washington, D.C. [13]
10/27/76	p. 245	Rufus Hallett Gardner III	1041 St. Paul St. Baltimore, Md.
	p. 307	Melinda Riegler Gravatt	230 Conwell St. Seaforth, Del.
	p. 351	Jackie Dean Gordon	10351 S.W. 5th St. Miami, Fla.
10/28/76	p. 410	Lawrence Vineburgh	4201 Cathedral Ave. N.W. Washington, D.C.
	p. 447	Rossana Nardizi	Federal Trade Commission Dallas, Texas
	p. 490	Concepcion Viera	1012 W. 24th St. Hialeah, Fla.
	p. 505–A	Virginia Cook	Box 142 Delmar, N.Y.
10/29/76	p. 501	Arnold Goodman	41 Crestview Dr. Willingboro, N.J.
11/3/76	p. 654	Lillian K. Zuccarelli	22 Lenmar Dr. Trenton, N.J.
Witnesses called by respondents were as follows:			
11/3/76	p. 742	Arnold Goodman	41 Crestview Dr. Willingboro, N.J.
11/4/76	p. 895	Andrea Absalom	1306 Cooper St. Beverly, N.J.
	p. 962	Anthony V. Pavlovich	413 Stonington Rd. Silver Spring, Md.
	p. 998	Norman Bricker	Millside Manor Delran, N.J.

The only witness called in rebuttal by complaint counsel was:

11/4/76	p. 1011	Arnold Goodman	41 Crestview Dr. Willingboro, N.J.

[14]

(2) *Evidentiary Rulings*

Most objections to proposed exhibits and testimony were ruled on as soon as made but in one instance the ruling was taken under advisement and must be made now.[9]

Debtor Witness Gordon retained counsel in connection with the underlying dispute which led to his being dunned by Capax and again in connection with Capax' dunning letters. The incident is developed at Tr. 356–372. After receiving Capax' initial mailing Gordon and his lawyer agreed that the lawyer would write Capax a letter warning that this was a disputed claim and that any credit information released by Capax should bear such a notation. See CX 62(b) ident. and Tr. 355, 357–8, 361. The trouble was that complaint counsel had no better copy of the letter than CX 62(b) ident., which was Gordon's unsigned carbon copy of an assumed original letter from the lawyer (one Nelson) to Capax, and they did not want to bring the lawyer all the way from Miami to identify this piece of paper.

CX 62(b) ident. was offered for the twin purposes of corroborating witness Gordon's reaction (fear for his credit standing) when he received Capax' first dunning letter [CX 62(a)] and to show Capax' inaction in response to the lawyer's letter (Tr. 370–371). Respondents objected vigorously that it was hearsay evidence, that a search of their own files led them to doubt that they had ever received the assumed "original" and that they had had inadequate notice of complaint counsel's intent to offer this copy if respondents would not or could not produce an original.

We are satisfied that the circumstances provided good cause for the timing of complaint counsel's offer but we have concluded that in the absence of testimony by Gordon's lawyer as to his actually sending off the letter to Capax, CX 62(b) ident. should be received only for the limited purpose of corroborating the feeling of fear for his credit standing to which Gordon testified on the stand. With that limitation, CX 62(b) is received in evidence *nunc pro tunc* as of 10/27/76. [15]

(3) *Motion for Direct Verdict*

At the close of complaint counsel's case in chief on 11/3/76 respondents moved for a directed verdict, which we treat here as a motion to dismiss the complaint for failure to make a *prima facie* case.

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[9] A recent brief denominated a "motion" opposing admission of CX 62(b) ident. submitted by respondents under date of 4/18/77 has received due consideration, as has complaint counsel's "Response, etc." dated 4/20/77.

Respondents filed a brief thereon and both sides argued the motion orally (Tr. 682–701). By virtue of Rule 3.22(c), we deferred acting on this motion until after the close of the case for the reception of evidence. (Tr. 740.) In view of our disposition of this case, said motion is now dismissed as moot.

F. POST-TRIAL MATTERS

There was some delay in the receipt of transcripts of the hearings and corrections required additional time. On 12/28/76 undersigned issued a formal order closing the record as of 12/13/76 in accordance with earlier informal discussions. On 1/24/77 both complaint counsel and counsel for respondents Capax, Inc., DeFelice and Goodman filed their proposed findings of fact, conclusions of law and order, with supporting briefs. Replies by respondents and complaint counsel were filed on 2/3/77 and 2/4/77 respectively. Counsel for respondent Bricker on 1/4/77 wrote the Commission, adopting his co-respondents' proposed findings with one exception and one addition and we have treated this letter as properly filed. On 3/8/77 the Commission granted the administrative law judge an extension of time until 4/13/77 within which to file this initial decision and on 4/13/77 extended said filing date to 4/22/77.

II

Findings of Fact

Respondent Capax

1. Respondent Capax, Inc. (hereafter sometimes "Capax"), until 1/21/75 known as Continental Credit Corp. [CX 30(b)], is a corporation organized on 2/2/72 [CX 60(n); CX 61(h)] which is still existent and doing business under and by virtue of the laws of the State of New Jersey, with principal office and [16] place of business at the intersection of Route 130 and Beverly-Rancocas Road, Willingboro, New Jersey. [Complaint ¶ 1; Answers, ¶ 1.] In these findings the name "Capax" is used to denote this corporation at any time of its existence, including the period when it was known as Continental Credit Corp.

Respondent DeFelice

2. Individual respondent Joseph V. DeFelice was a major shareholder of Capax, owning about 31 percent of its shares, [CX 5] until he sold his interest in Capax to respondent Arnold Goodman in July 1976. [Tr. 503–504]. DeFelice was the only Chairman of the Board from the corporation's organization in February 1972 [Tr. 230] and Treasurer

from February 1972 to July 19, 1976 [Tr. 502]. From the start of the corporation in February 1972 until said DeFelice's resignation in July 1976 as an officer and director [Tr. 220] he was a principal owner and officer of Capax, who formulated, directed and controlled its acts and practices, including those set forth in this complaint. [Complaint, ¶ 1 and Answers, ¶ 1.] His present association with Capax is that of a vendor of data processing services (Tr. 504).

Respondent Goodman

3. Individual respondent Arnold Goodman has been a major shareholder of Capax since it was organized in February 1972, owning about 31 percent of its shares [CX 5] until he purchased respondent DeFelice's interest in July 1976, thus raising his (Goodman's) holdings to about 62 percent of the corporation's total shares. [Tr. 503–504]. Respondent Goodman has been President of Capax since February 1974 [CX 61(h)]. As a principal owner and officer of Capax he has formulated, directed and controlled its acts and practices, including those set forth in this complaint. [Complaint ¶ 1 and Answers ¶ 1.]

Respondent Bricker

4. Individual respondent Norman Bricker was a major owner of stock (31 percent) [CX 5 and Tr. 1003] and [17] Executive Vice President of Capax from the time of its organization in February 1972 until March 19, 1975, when he terminated his connection with the corporation [CX 6(a) and Tr. 1000]. As a principal owner and officer of Capax he generally participated in the formulation, direction and control of its acts and practices. [Letter of Bricker's counsel to Secretary of Commission, filed 2/4/77, in lieu of formal proposal of findings.]

5. Despite respondent Bricker's denial that he participated in formulating the language used in any of Capax' dunning letters (Tr. 999, 1004) and assertion that he was in charge of selling a service, not letters, except as part of the service (Tr. 1003–1004), there was contrary testimony by respondent Goodman that Bricker was instrumental, with his two "partners" in putting together at least dunning series CX 10 and CX 11 [Tr. 507, 607, 640, 644, 648–9]. We now find that in addition to his overall responsibility as a major owner, Executive Vice President and Sales Manager, respondent Bricker actually participated with other respondents in many of the acts and practices set forth in this complaint.

Capax' Business

6. Since the inception of Capax' business, it has been engaged in

advertising, offering for sale and selling a service to assist creditors in the collection of alleged delinquent debts. [Complaint ¶ 2 and Answers ¶ 2.] This service has consisted primarily (and until about 3/18/75 solely) of a "flat rate" arrangement for mailing by Capax of a series of dunning notices to alleged delinquent debtors at regular intervals [Complaint ¶ 2 and Answers ¶ 2; Tr. 506–7]. The parties have stipulated that a "flat rate debt collection service" involves "a sale at a specified fee (flat rate), non-commission basis of a service constituting (constituted?) in part of the preparation and sequential mailing of a series of notices. There is no legal assignment of the claim of debt by the creditor to the seller of the service during the course of the service." (Tr. 243–4). [18]

7. Capax' authority to act for creditors is not unlimited [Tr. 528]. It is derived from an "Authorization To Start Service" (CX 27) and a "Receipt" (CX 33). It offers clients several different kinds of dunning service. It has long and short versions of a "strong" series, a "diplomatic" series, a "bad check" series and a Spanish language series. See the following series:

CX 10(a) - "Diplomatic" (long and short)
CX 11(a) - "Strong" (long and short)
CX 12(a) - "Spanish Language, Diplomatic" (long and short)
CX 13(a) - "Spanish Language, Strong" (long and short)
CX 14(a) - "Special" (bad check; reinstate) (strong and diplomatic)
CX 15(a) - "Special" (bad check, reinstate) (strong and diplomatic)
CX 16(a) - "Special" (bad check, reinstate) (strong and diplomatic)
CX 17(a) - "Diplomatic" (for reinstatement after default)
CX 18(a) - "Strong" (for reinstatement after default)
CX 19(a) - "Spanish Language, Diplomatic" (for reinstatement after default)
CX 20(a) - "Spanish Language, Strong" (for reinstatement after default)
CX 21(a) - "Bad Check"

Capax' charges were about $3.84 per series when the business started and later about $4.25 [Tr. 512, 794–796].

8. Capax sells its dunning service as part of a more comprehensive "credit control system consisting of sending out the letters, generating reports and advice and helping to control the receivables for the individual company" [Tr. 504, *et seq.*]. It advises the creditor concerning the taking of further stronger actions when it returns a list of debtors unsuccessfully dunned. (Tr. 562, 603, 766–8, 798–800, CX 4.) Its "prime function" is to get the money paid to the creditor. . . . not

selling letters." [Tr. 513]. **[19]** Complaint Counsel's Reply Findings [Par. # 6] stress the "self-serving" nature of Capax' testimony about analyzing delinquent accounts receivable and advising creditors how to minimize their losses, etc. However, complaint counsel offered no contrary testimony by creditor-clients or others and we see nothing inherently improbable about the testimony of Mr. Goodman, the principal witness on this subject [Tr. 504–516].

9. Capax is licensed to receive payments in the five or six states where it can do so [Tr. 761] but debtors are always requested, at least in flat-rate dunning, to make payment directly to their creditors [See CX 10 series, *et seq.*] Despite this caution, however, about 2 percent of all collections (about $20,000 in the 1973 period) (Tr. 241) are usually sent to Capax, which immediately forwards such monies to the creditor-client [Tr. 881–882]. Clients have never objected to getting their money this way [Tr. 529].

10. Since about 5/1/75 Capax has offered an additional and more forceful collection service, which it calls its "second phase" for those "hard core" cases where the flat rate letter writing service has been unsuccessful in effecting collection of a debt. [Tr. 555–578, 790, *et seq.*] As part of "Phase II" dunning, phone calls may be made to the debtor [Tr. 553] and the claim may even be turned over to an attorney for suit, unless the creditor gives Capax specific orders to the contrary [Tr. 555, 802]. "Phase II" also differs from flat-rate dunning in that there is a more expensive, percentage fee for this supplementary service [Tr. 796] and the debtor is asked to pay Capax rather than the creditor [Tr. 556].

11. Even now, however, Capax' contractual arrangements with its creditor-clients do not provide for it to bring suit, either in its own name or the creditor's name [Tr. 530] It has, in fact, never brought such a suit against anyone [CX 60(q)–CX 61(j)]. It is not authorized by law to bring such suits [Tr. 556, 793, 794]. State laws allow only the creditor to sue the debtor [Tr. 793–794] and Capax does not ordinarily take assignments of the debts referred to it [Tr. 824]. **[20]**

Interstate Commerce

12. All Capax' forms of notices sent to debtors in connection with its flat-rate debt collection service have been mailed from its home office in Willingboro, New Jersey. [CX 60(p) and CX 61(i)]

13. Capax sells and at least since February 1974 has sold its flat rate debt collection service thru its salesmen, all of whom sell on commission (Tr. 779–800), in the States of New Jersey, New York, Pennsylvania, Massachusetts, Vermont, Maryland, Florida, Louisiana, Rhode Island, Michigan, New Hampshire, North Carolina and the

District of Columbia [CX 60(o) and CX 61(i)] and thru so-called "charter agents"[10] in the same states plus Ohio less New Hampshire and Rhode Island [CX 60(p) and CX 61(i)].

14. The approximate dollar volume of sales of Capax' flat rate debt collection service between 2/2/72 and 1/25/75 was not insubstantial [CX 60(p) and CX 61(i)] nor was its dollar volume of sales from 1/26/73 to 6/30/75 [CX 60(p) and CX 61(i)]. Between 1/1/73 and 5/6/74, for example, its dollar volume of sales was about $700,000 [CX 1(e); CX 3(b)]. Collections realized by creditor-clients were of a higher order: *e.g.* approximately $10,000,000 during the 12 months ended October 1973 (Tr. 881–882).

15. Capax' dunning of alleged debtors in many states from its headquarters in New Jersey by use of the U.S. mail constitutes and has constituted at all relevant times a course of trade in and affecting commerce, as "commerce" is defined in the Federal Trade Commission Act [Complaint ¶ 3, Answers ¶ 3].

Alleged Deceptive Appearance

16. From the inception of the business in February 1972 until October 1973 (a little more than three months before receiving notice of the investigation that preceded issuance of this complaint) when an [21] "impact" dunning message seemed called for, Capax used something that looked a great deal like and, indeed was actually captioned a TELEGRAM. This will readily appear from inspection of the initial and certain other letters in each of the CX 17, CX 18, CX 19, CX 20 and CX 21 series as well as from inspection of CX 22(b), a sample of the envelopes in which such letters were sent. All are admitted to be representative samples of forms and envelopes sent to debtors by Capax via the U.S. mail prior to 10/10/73, about which time the use of this TELEGRAM form was abandoned by Capax on advice of counsel as a result of the proposed consent order (later rejected) in the Commission's still pending proceeding in the matter of *Trans American Collections* [CX 60(q) and CX 61(j)].

17. Although none are, in fact, telegraphic communications [CX 60(r) and CX 61(j)] the administrative law judge has little doubt that the word TELEGRAM in large, standout type on a yellow paper (with brown bar across the top), of the size and shape of a Western Union message form, and printed in similar type, would be hard for many people to distinguish from a real telegram. This complaint, however, makes no charge of deception with respect to these "TELEGRAMS," presumably because of the abandonment of their use in October 1973.

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[10] For an example of a "charter agreement" see CX 28(a) thru CX 28(t).

18. Since then Capax has used a different appearing form called a LETEGRAM for its "impact" dunning letters. Representative samples of letters sent out by Capax to debtors via the U.S. mail in the course of its flat-rate service since 10/10/73 are found in the initial and other letters of the CX 10, CX 11, CX 12, CX 13, CX 14, CX 15 and CX 16 series of exhibits [CX 60(q) and CX 61(i)] and CX 22(c) is a sample LETEGRAM envelope. [Ibid.]

19. As will readily be seen from visual inspection, the LETEGRAM format constitutes a major change, not only in its very prominent caption — now LETEGRAM instead of TELEGRAM— but in its color scheme: a gray paper with a striking reddish purple bar across the top, which we find would be most unlikely ever to be mistaken for a Western Union telegram. [22]

20. Complaint counsel contend that this LETEGRAM on gray paper with a reddish purple bar is still confusingly similar to a real telegram, because, they claim [CPF 11], 3 of their 9 debtor witnesses testified that they were thus confused and a Massachusetts state official has refused to authorize use of LETEGRAMS in that state as "potentially deceptive" [CX 31(a)]. We start, however, with a contrary view from our own inspection of the documents, fortified by the adverse inference we must draw from Complaint Counsels' failure to ask 6 of their 9 witnesses — sifted from some 2000 prospects [Prehearing Order # 3] — whether they really believed the LETEGRAMS they received from Capax were telegrams.

21. As for complaint counsel's three alleged supporters among the witnesses, the first, Ms. Gravatt, was neither shown nor questioned about a LETEGRAM and, indeed, affirmatively testified that she received a yellow paper captioned TELEGRAM, identifying CX 21(b) and CX 22(b) (both with TELEGRAM format) as similar to what she received [Tr. 310–311]. Of the two other witnesses relied on to establish that some people may confuse LETEGRAMS with TELEGRAMS, one, Ms. Cook, had for 16 years been the manager of a collection agency in Albany [Tr. 505–A] where Capax, too, maintains an office [CX 11(r)] and she stressed her humiliation at getting her first dunning letter from a collection agency [Tr. 513–A], a background we cannot disregard in weighing her testimony that she was "not in the habit of getting telegrams," "didn't notice it said LETEGRAM" and "thought it was a telegram." [Tr. 508–A and 509–A]. The only other supporting witness, Ms. Nield, a student of consumer economics [Tr. 165], testified for the prosecution that she had gotten an "initial impression" that her LETEGRAM "appeared to be a telegram or a Western Union letter or gram or whatever" [Tr. 148–149]. Whether her "initial impression" was more than momentary was not brought out.

22. We find that Capax' LETEGRAM, as distinguished from its earlier TELEGRAM, is unlikely to deceive ordinary debtors into believing they have received a real telegram. Moreover it is unlikely to deceive any [23] debtor more than momentarily and certainly not long enough to affect any action. That the use of LETEGRAMS is viewed as deceptive by a Maine official [CX 31(a)] — although not in any of the dozen other states where Capax operates — cannot control our finding here.

23. Our finding that the ordinary debtor is not likely to be deceived by a LETEGRAM into thinking he has received a real telegraphic message disposes also of the second-step charge of this complaint that an appearance simulating telegraphic or other similarly urgent communications, "*by virtue of said simulation*" tends to mislead the recipient as to its "nature, import, purpose and urgency" (Complaint, ¶ 6). Even though the appearance of a dunning letter may be made similar enough to a telegram to stimulate a conditioned emotional response of urgency and importance, as long as the recipient is mentally aware that he got a gimmick, not a telegram, there is not the deception which turns a Harvard Business School market research problem into a Federal Trade Commission unfair trade practice case. In the absence of a finding of capacity or tendency to deceive, why one method of persuasion is more effective psychologically than another is not a concern of this Commission. Accordingly, we find that the appearance of Capax' LETEGRAM did not tend to *deceive* debtors as to the "nature, import, purpose or urgency" of the message therein.

The "Collection Agency" Image

24. Complaint Pars. 9.1 and 9.2 allege that by styling itself a "collection agency" Capax, a mere dunner, tries to deceive debtors into believing Capax is a full-line[11] collection agency which may file [24] collection suits and take other actions Capax does not (or did not) take before 5/75. It is charged, in short, that Capax is a sheep in wolf's clothing.

25. The extracts from its dunning letters alleged to prove that it represents itself as a "collection agency" are found in CPF # 50. Complaint counsel point to the use of the phrase "CREDIT CONTROL AND COLLECTION" in most of Capax' non-TELEGRAM letterheads (See CX 10 series thru CX 21 series) plus use of the words "Collection Dept." under

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[11] Complaint Par. 8.1 does not use the word "full-line" but seems to use the word "independent" in that sense. Both sides do use the word "independent" but use the word in different senses. The normal meaning, we would think, is respondents' meaning: that Capax is not owned or operated by any creditor, as was the case in *Wm. H. Wise Co., Inc.*, 53 F.T.C. 408 (1956); *affd. per curiam*, *Wm. H. Wise Co., Inc.* v. *F.T.C.*, 246 F.2d 702 (D.C. Cir., 1957), *cert. den.*, 355 U.S. 856 (1957). By "independent," however, complaint counsel apparently mean an agency to whom a creditor has delegated the maximum possible authority to collect its debts. There was no evidence of industry terminology in this respect and we think it more meaningful to use the word "full-line" instead of Complaint Counsel's "independent."

the signature in various communications [CX 19(g)-(l), CX 11(h)-(j), CX 16(b)-(c), CX 17(g)-(j), CX 18(f)-(h)]. We find these examples clearly establish that Capax represents itself as a "collection agency."

26. On the other hand, we are not convinced that such a representation is false. It all depends on how one defines the word "collection" and the Commission's own definition [16 C.F.R. 237.0(f)] really begs the question. Defined literally, it might include only businesses that receive payments from debtors but Capax would pass that test. Although its dunning letters regularly ask the debtor to make payment directly to the creditor, there are always some debtors who channel payment thru Capax. These receipts amounted to about $20,000 or .2 percent of all collections in a period of a year. [Tr. 881–882] Capax is officially licensed to receive such payments wherever it can lawfully do so. [Tr. 761] [25]

27. If "collection" must include the bringing of collection suits, then it would have to be acknowledged that Capax has never been a "collection" agency, for it has never brought suits, either for its clients or in its own name [Tr. 530, CX 60(e)-CX 61(j)]. But complaint counsel, on whom always rests the burden of proof, offered none that the bringing of "collection suits" is viewed in the industry or elsewhere as a *sine qua non* for a "collection agency."

28. The significant fact is that Capax' principal activity, dunning debtors (by mail during its entire existence and by telephone since early 1975) is a very important element of the overall "collection process," as it is called by a Maine official in one of complaint counsel's exhibits [CX 31(h)]. Indeed, complaint counsel themselves find it natural enough to refer to Capax' "flat rate debt *collection* service" (emphasis added). [See CPF, p. 7 (heading) and CPF # 24 (last full line).] One of their witnesses, a 16-year veteran of the collection business, called Capax "a collection agency or whatever" (Tr. 513-A). It seems to us that a dunning agency is as much a part of the "collection process" as a collection attorney or others who may perform other of the various functions which make up the whole collection process. Accordingly, we find that simply by styling itself a "collection" agency on letterheads or under signatures Capax did *not* misrepresent the true state of things and therefore deceived no one.

29. Complaint counsel do not, however, rely entirely on Capax' *expressly* styling itself a "collection" agency. In their proposed findings (CPF # 50, 53) they cite extracts from Capax dunning letters which they assert would *imply* to debtor recipients that the alleged debt in each case had been referred to respondent as a third party, totally "independent" of the creditor, which would engage in any action necessary to induce payment of the alleged debt (CPF # 51) or as an

assignee of the account (CPF # 53). We find, however, that the language of the extracts cited in support of this argument was simply a natural introduction and/or explanation of why Capax had to get in touch with the debtor and we find further that it did *not*, in fact, operate to deceive debtors, as Complaint Counsel assert. Indeed, the cited extracts [26] of debtor testimony on which complaint counsel rely to show actual deception (in order to establish a capacity to deceive) affirmatively establish that it was *other* language in the dunning letters than these introductory explanations which allegedly led them to believe they would be sued, etc. Concrete examples will help to make this clear.

30. The testimony of Ms. Thom (Tr. 136) that she was led to fear suit by Capax is cited in support of the deceptive nature of three introductory explanatory passages quoted in CPF # 51:

> *CX 18(b) et al.:* [Creditor] has turned over to us their claim against you for $9999.99. . .
>
> *CX 18(c) et al.:* You have failed to discharge the debt submitted to us for action by [Creditor]. . .
>
> *CX 18(d) et al.:* [Creditor] has charged us with the responsibility of assisting the liquidation of their past due accounts. . .

It is complaint counsel's theory that such introductory explanatory language misled Ms. Thom and other debtors into believing they were being attacked by a full-line collection agency which could bring suit and do other frightening things that Capax could not do. On the witness stand Ms. Thom did, indeed, insist that despite absence of the word "suit" in any of the three dunning letters she somehow got the idea she was going to be sued.

31. When shown such letters, however, the language in which Ms. Thom took refuge was no statement that the claim had been turned over to Capax but that Capax was going to do certain things. In CX 18(b), for example, the language to which she looked was: "If not paid within one week, to liquidate this matter we will be forced to recommend action." (Tr. 128) In CX 18(c) she pointed to the language "It is the intention of our client to exhaust every legal means at their disposal." (Tr. 128) In [27] CX 19(d) she referred to the language: "And of the fact that should it continue, all possible legal means will be taken to collect it," etc. (Tr. 130). Plainly it was the mention of the creditor's turning the claim over to Capax which led Ms. Thom to believe she was going to be sued.

32. The case of debtor witness Nield is similarly cited. She was shown CX 14(b), which reads in part:

> And your account has now been turned over to us for action.

Asked what this meant to her when she received it, Ms. Nield replied: "Just that, that [Capax] was now collecting from me, that Sears had. . . contacted Capax to obtain payment" (Tr. 171). Yet when asked: "Did anything in the communication [CX 14(b)] indicate suit or (adverse effect on) credit which you felt might happen?" (Tr. 150), Ms. Nield did *not* refer to the language about her account now being turned over to Capax for action, but to other language, all in a different paragraph, about "legal ramifications and the exercising of the legal means to recover the loss." (Tr. 151 and 154).

33. Debtor Witness Zuccarrelli received from Capax, a dunning letter [CX 11(c)] with the usual introductory explanation: "[Creditor] has turned over to us their claim against you for $9999.99. . . ." It went on to say that if this account be not paid within one week Capax would be forced to recommend action, which might mean added costs, etc. Although CX 11(c) refers to the creditor's turning over his claim against Ms. Zuccarrelli to Capax, it was not to that statement but to an entirely different one that Ms. Zuccarrelli twice referred when asked what part of the letter led her to think she was about to be sued:

> Q. . . . (W)hat language in that particular letter [CX 11(c)] made you believe you would be sued? [28]
>
> A. "Recommend action which may mean added costs to you." Action, court action, is what I took it for" (Tr. 679)

34. Debtor Gravatt is another witness cited on this point in CPF # 51 and # 54. She had received CX 21(b), a dunning letter which included the words "and your account has now been turned over to us for action." When first questioned about her reaction to the letter on direct examination she testified to feeling that "someone was either going to come to my door and ask me for the money or I would have to go to Court to pay for the (bad) check." (Tr. 311). She gave as her reason for believing she would be taken to court that "it [CX 21(b)] said they had turned (the) account, or whatever, over to [Capax]" (Tr. 311). This testimony, untested, might conceivably support complaint counsel's theory that merely believing Capax to be a full-line collection agency would lead a debtor to expect to be sued, hounded, discredited, etc.

35. Persistent cross-examination, however, obtained a significant reversal of the testimony which young Ms. Gravatt had given in the hands of complaint counsel. She first decided that she would have to say it was "the whole thing" [*i.e.* all of CX 21(b)] that led her to expect either suit or a personal visit from a collector (Tr. 322). Next she conceded that her fear of a visit by someone from Capax was really

related to different words in CX 21(b), to wit, "Our client can exercise all legal means to recover the loss."[12] (Tr. 323). Finally she tied the same passage ("exercise all legal means") to her fear that if she didn't pay, she would have to go to court." (Tr. 346). The truth which emerged on cross-examination, supports the same conclusion as that of the debtor witnesses just reviewed: what concerned these debtors was not the fact of turnover but specific actions thereafter threatened. [29]

36. Witness Gardner assumed that "any action" brought would be instituted, at least, by Capax because Capax had indicated throughout that the claim had been referred to it for action. However, that is quite different from complaint counsel's argument that the recital of referral to Capax would lead a debtor to expect suit. (Tr. 263). Gardner came as close as any witness to adopting complaint counsel's theory when he said "I felt that this letter [CX 29(d)] after all, this letter coming to me from an agency is itself a threat," "Take some kind of action." However, he went on to concede that it was the document's mention of "credit" which led him to assume the threat was going to focus initially on his credit (Tr. 287). Moreover, Gardner's righteous zest for battle with his creditor [Tr. 295–296] had to color all his retrospective analyses of how he felt about Capax' tactics. We find him to be no ordinary debtor.

37. Careful study of the testimony of the few other debtor witnesses cited in CPF # 51 and CPF # 53 reveals mostly confusion, such as witness Gordon's confession that after reading CX 62(a) he was "not sure" what action was going to be taken (Tr. 355). Ms. Cook's conviction, as a professional debt collector that nobody would actually sue her over a $20 claim [Tr. 516–A] makes her testimony as to whether she might otherwise have expected a law suit pure speculation. [CX 514A, 516A, 517A] In any event the others fail to make the convincing showing which complaint counsel's burden of proof requires.

38. We are satisfied from these illustrations as well as from simple common sense that a mere introductory explanation in Capax' dunning letters that the creditor involved had turned his claim over to Capax for its action in itself had no significant tendency to make debtor recipients assume they must be going to get the full treatment. If such debtors concluded — rightly or wrongly — that they were going to be sued and/or that their credit would be ruined, it was rather on the basis of much more pointed representations in Capax' dunning letters concerning what was going to happen to the debtor and to those more significant representations we now turn. [30]

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[12] We quote the witness' version of what CX 21(b) said. The correct wording of the quoted sentence was really: ". . . we will have to recommend that our client exercise all legal means to recover this loss."

Accordingly, we think it more profitable to forego further discussion of complaint counsel's exercise in scholastic logic and proceed directly to consideration of those representations which complaint counsel's own debtor witnesses say led them to believe that they would be sued or that their credit would be ruined.

Threats of Suit

39. In proof of complaint Pars. 8.2 and 9.2, which are really the crux of this litigation, complaint counsel first point to 11 examples of texts taken from Capax dunning letters. These, they believe, would give debtors an impression that if payment were not received, suit definitely *would* be filed or some other legal action definitely *would* be taken against the debtor (by whom is not alleged). (CPF, p. 15) Our own inspection of the face of these selected texts indicates that some do and some do not support complaint counsel's assertion.

40. We find that the first half of these extracts, fairly read, made a definite threat of suit (sooner or later), conditional only on nonpayment of the debt. These extracts are as follows:

> . . . IT IS THE INTENTION OF OUR CLIENT TO EXHAUST EVERY LEGAL AVENUE AT THEIR DISPOSAL IN ORDER TO COLLECT THIS CLAIM. (sixth, second, eighth and second contacts), respectively, Diplomatic and Strong series, CX 10(i); CX 11(d); CX 17(h); CX 18(c); Spanish series, CX 12(j); CX 13(d);
>
> IF YOU PERSIST IN NOT FOLLOWING THROUGH YOUR OBLIGATION, WE WILL HAVE TO RECOMMEND A MORE DRASTIC ACTION THAT IN THE END WILL BE MUCH MORE COSTLY TO YOU. IF THIS IS YOUR INTENTION, I WOULD RECOMMEND THAT YOU CONTACT YOUR ATTORNEY, SO HE MAY ADVISE YOU ON THE LEGAL RAMIFICATIONS YOU MAY BE EXPOSED TO. (sixth and eighth contacts), Diplomatic series, CX 10(i); CX 17(h); Spanish series, CX 12(j); CX 19(h); [31]
>
> IT IS IMPERATIVE THAT YOU CONTACT YOUR CREDITOR TODAY TO AVOID FURTHER ACTIONS. . . (fifth, sixth and second contacts), respectively, Diplomatic and Strong series, CX 10(g)-(h); CX 17(g); CX 18(c); Spanish series, CX 12(h)-(i); CX 13(d);
>
> . . . IMPERATIVE THAT SATISFACTORY ARRANGEMENTS BE MADE TO AVOID FURTHER ACTION, AVAILABLE TO CLAIMANT UNDER PROVISIONS OF STATE STATUTES. . . (seventh contact, Diplomatic series, sixth contact, Strong series), respectively, CX 10(j)-(k); CX 11(i)-(j); CX 18(h); Spanish series, CX 12(k)-(l); CX 13(k); CX 19(i); CX 20(h);
>
> . . . IF YOU WANT TO AVOID UNPLEASANT AND COSTLY ACTION, MAKE IMMEDIATE PAYMENT DIRECTLY TO A-B-C- SUPPLY COMPANY
>
> * * * * * * *
>
> IT WOULD BE MOST UNFORTUNATE FOR YOU TO MAKE IT NECESSARY FOR

A-B-C- SUPPLY COMPANY TO TAKE MORE FORMAL ACTION, FOR YOU MAY BE OBLIGED TO PAY LEGAL COSTS AND INTEREST CHARGES IN ADDITION TO THE $9999.99 YOU OWE. . . (eight contact, Diplomatic series, sixth contact, Strong series), respectively, CX 10(l); CX 18(g); Spanish series, CX 13(i); CX 19(j); CX 20(g);

YOUR REFUSAL OR NEGLECT TO SATISFY THE ABOVE LIABILITY COMPELS US TO NOTIFY YOU TO PRESENT ANY DEFENSE AGAINST THE VALIDITY OF THIS CLAIM ON FILE. YOU MAY PROTEST SAID CLAIM OR LIST PROPERTY WHICH YOU FEEL MAY BE EXEMPT, IF A-B-C- SUPPLY COMPANY OBTAINS A JUDGMENT. (ninth contact, Diplomatic and Strong series, tenth contact, Diplomatic and Strong series), respectively, CX 10(m); CX 11(n); CX 17(k); CX 18(k); Spanish series, CX 12(n); CX 13(m)-(n); CX 19(k); CX 20(j); [32]

WE ARE WRITING THIS LETTER TO INFORM YOU OF THE SERIOUSNESS OF YOUR DELINQUENCY AND OF THE FACT THAT, SHOULD IT CONTINUE ALL POSSIBLE LEGAL MEANS WILL BE TAKEN TO COLLECT IT. (third contact, Strong series), CX 11(e); CX 18(d); Spanish series, CX 13(e); CX 20(d);

41. We find, however, that the last half of the extracts, fairly read, make no such threat of suit but are only a fair reminder that the creditor *may* have to initiate legal action if payment is not forthcoming. These extracts are as follows:

IF THIS IS NOT DONE CONTINENTAL CREDIT CORPORATION CAN TAKE NO OTHER POSITION BUT TO RECOMMEND A STRONGER COURSE OF ACTION TO OUR CLIENT. . . IF THIS IS DONE THERE MAY BE ADDITIONAL COSTS TO YOU. . . (fourth contact, Strong series), CX 11(f)-(g); CX 18(e); Spanish series, CX 13(f)-(g); CX 20(e);

. . . YOU LEAVE NO OTHER AVENUE OPEN TO US. A-B-C- SUPPLY COMPANY IS ABLY REPRESENTED BY LEGAL COUNSEL WHO, IF CALLED UPON, WILL PURSUE THE APPROPRIATE LEGAL MEANS TO LIQUIDATE THIS OUTSTANDING DEBT. . . SHOULD JUDGMENT BE TAKEN AGAINST YOU, THE COURT MAY CHARGE YOU FOR LEGAL COSTS AND FEES. . . (fifth contact, Strong series), CX 11(h); CX 18(f); Spanish series, CX 13(h); CX 20(f);

. . . IF PAYMENT IS NOT RECEIVED IN THE ALLOWED TIME, AND COUNSEL COMMENCES LITIGATION, YOUR CREDITOR MAY ALSO BE AWARDED EXPENSES AND LEGAL COSTS BY THE COURT. (seventh and eighth contact), respectively, Strong series, CX 11(k); CX 18(i); Spanish series, CX 13(l); CX 20(i); [33]

. . . FAILURE TO COMPLY AND APPEAR EITHER IN PERSON OR HAVE LEGAL REPRESENTATIVE ATTEND ON YOUR BEHALF MAY RESULT IN START OF LEGAL ACTION BY A-B-C- SUPPLY COMPANY. . . (eighth and ninth contacts), respectively, Strong series, CX 11(l)-(m); CX 18(j);

IT IS IMPORTANT THAT YOU MAKE YOURSELF AWARE OF THE LEGAL RAMIFICATIONS OF THIS TYPE OF PRACTICE. . . . IF YOU DO NOT CORRECT THIS MATTER QUICKLY, WE WILL HAVE TO RECOMMEND THAT OUR CLIENT EXERCISE ALL LEGAL MEANS TO RECOVER THIS LOSS. . . (first contact, Bad check series), CX 14(b)-(c); CX 21(b); Spanish series, CX 14(d)-(e);

42. In addition to examining these texts on their face, we must

consider the testimony of five debtor witnesses presented by complaint counsel concerning their reactions to the same or similar texts. All five claimed that the texts they received definitely threatened suit in the event of non-payment, notwithstanding our reading of four of these texts to warn only of a possibility of suit [Gravatt, Tr. 321–2, re CX 21(b); Nield, Tr. 151, 154, re CX 14(b); Gardner, Tr. 263, re CX 29(q), (see equivalent CX 10(m)); Vineburgh, Tr. 437, re CX 11(b)]. In the case of one debtor witness the debtor's reaction was the same as ours (from the face of the documents) that there was a definite threat of suit in the event of non-payment. [Thom, Tr. 128–130, re CX 18(c) and CX 18(d).] Although examination of the face of these dunning letters supports the debtor-witness testimony in only one out of five instances, there is no escaping the fact that half of the texts must be read on their face as definitely threatening suit, unless payment be made.

43. Complaint counsel have thus established a *representation* that Capax' creditor-clients would bring suit if necessary to get their money — but was it a *misrepresentation?* Complaint Par. 9.2 pleads [34] that, in truth and in fact, "if payment was not received, steps were not taken to initiate legal action against the alleged debtor (and) in fact, no action was taken during the form letter series except to send additional form letters to the alleged debtor or to return the uncollected account to the creditor." The joint answer *denied*[13] that Capax does *not* "take steps to see that legal action is initiated, provided that the debt remains unsatisfied and no instructions are received from the creditor not to do so at that time." The *burden of proof* was thus on complaint counsel to establish a negative proposition, to wit, that Capax does *not* take steps to see that legal action is initiated, etc. before Capax' representation could become a misrepresentation.

44. Complaint counsel sought to carry their burden in the following way. Firstly they asserted (CPF # 25) — and we now find — that Capax has never had either right or authority to bring suit against any debtor, either in its own name or in behalf of any other person or corporation, even after 5/75 when it went beyond letter-writing to add a more vigorous "second phase," which, however, still omits suit. [See Finding # 11.] Respondents do not claim otherwise [RPF # 8]. It is thus clear that Capax itself did not, in fact, bring suits against debtors but there is nothing wrong with that unless there had earlier been a representation that Capax *would* bring such suits.

45. Most of the extracts from dunning letters on which complaint counsel rely to show threats of suit (see above) are plain on their face that they refer to a suit by the creditor, not a suit by Capax. They refer

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[13] The denial is confusingly worded: "admit they do. . . . take steps, etc."; but it is clear that a denial of a negative is intended.

explicitly to the creditor or to the fact that Capax will be making a "recommendation" or to some other clear indication that Capax would not be the plaintiff in such a suit. Those rare dunning [35] letters, like CX 11(e), which are silent on who will sue, must be read in light of the rest of the series and the complete absence therein of *any* reference to suit by Capax. While there was a little testimony by a few debtor witnesses as to some kind of impression that the dunning letters said they would be sued by Capax, we find no ambiguity in the comprehensive documentary evidence which would permit us to refer to such plainly erroneous debtor testimony. A witness cannot make black white just by becoming a debtor. We find that Capax never threatened in its dunning letters that it (as distinguished from its clients) would bring suit to collect a debt. Since it never threatened to bring suit itself, its lack of authority to bring suit becomes academic and the real issue finally emerges: Did Capax in any way misrepresent the likelihood that its *client* would bring suit to collect such debt?

46. Complaint counsel make a simple argument that it has to be misrepresentation for Capax to tell debtors they will definitely be sued in the event of non-payment, because Capax cannot know in advance what a particular client will ultimately do about bringing suit. (CPF # 57.) Indeed, complaint counsel several times extracted an admission from Capax' President Goodman that at the time a dunning letter goes out with a warning that Capax would sue the debtor if payment were not forthcoming Capax could not really say *"for a fact"* that this *particular* creditor would bring suit if the debt went unpaid [Tr. 543, 588, 590].

47. Goodman, on the other hand, claimed that Capax had a reasonable basis for sending such warnings in its broad experience with creditors and debtors generally and the involved creditor in particular. The following extracts from his testimony explain Capax' position.

> Q. Now you state [in CX 10(i)] that "It is the intention of our client to exhaust every legal avenue". How did you know at the time you wrote that letter that it was your client's intention to exhaust every legal avenue? [36]
>
> A. I have conversed with, talked with many of our clients as well as our people have (done so too) and *I have yet to find any of our clients that will not or do not want to get the money in and will not pursue it as far as they can to get it in.* Normally, if they would not want to, we would eliminate something like this from their contacts.
>
> Q. But you don't (didn't) know at the time you wrote that [CX 10(i)] what their intent really was, do you? Is it possible for you to know?
>
> A. *Normally we assume they want the money in and will follow through with all of the*

means they have to do it or they would not be asking us to do it. (Tr. 567) (emphasis added)

And similarly with reference to CX 11(e):

Q. . . . How do you know all possible legal means will be taken?

A. As I stated before, due to the knowledge and contacts of our (creditor) clients, *it is the intention of most of them to take all of the means at their disposal* to receive and get in the money owed to them.

Q. You are very specific when you use the words 'will be taken' and again the question is, at the time you wrote the letter, did you really know that in fact that will be done?

A. *This is normally implied to us by the creditor*, yes, sir. (Tr. 587-588) (emphasis added)

Again with reference to the same dunning letter [CX (11)(e)]: [37]

A. . . . (Y)ou really don't know whether the *particular* creditor. . . will in fact take every legal means available to him to collect the debt, including suit?

A. *We are under the impression given to us by our (creditor) clients that they would do this when financially feasible to do so.*

Q. What information do you have upon which to base this assertion?

A. Our contacts with our clients.

Q. I just asked you if you had records to indicate that all creditors sue all debtors after expiration of the service?

* * * * * * *

A. No.

Q. Again let me ask the question: When you write this letter you do not know whether in fact the *particular* creditor will take all possible legal means against the debtor to collect the alleged debt; do you?

A. *Normally this is implied to us that where it is financially feasible they will do that. This is their intention at the time.*[14] (Tr. 589–590) (emphasis added)

48. Mr. Goodman's qualification as to "financial feasibility" makes a finding as to the operative facts somewhat more difficult, because the record is bereft of testimony as to whether and, if so, under what [38] conditions costs of suit may make it unprofitable to bring a collection suit. CX 4, a sample "done" sheet for an "Elaine Powers Salon," reveals 15 bills ranging from $26.00 to $57.00 but there is no

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[14] Thereafter complaint counsel again obtained an admission that Goodman did not "know" this about a particular creditor.

way of knowing how typical they are. Of the 9 debtor witnesses who testified here, 5 were dunned for much larger sums,[15] while 4 were dunned for sums comparable to those found in CX 4 or even smaller.[16] In any event the other data needed to estimate what debts, if any, are too small to make suit worthwhile is completely missing from the record. Since the burden of proof is always on complaint counsel, we feel compelled to hold that in the absence of proof as to the magnitude and effect of the "financial feasibility" factor, it must be assumed to be of negligible significance for present purposes.

49. Accordingly, we now find that while Capax did not regularly make inquiry of or obtain knowledge from particular creditors as to their intentions to bring suit against particular debtors if the latter should fail to respond to Capax' dunning letters and while in that sense Capax did not "know" what such creditors would do, it did have a *reasonable basis* for warning debtors to expect suit if they did not pay up, in its knowledge from experience that creditors generally and Capax' clients in particular, almost without exception, want to sue for their money if necessary, assuming a negligible economic feasibility factor. [39]

Threats To Credit Standing

50. In proof of complaint Pars. 8.3 and 9.3, which allege that Capax falsely threatened to adversely affect debtors' credit ratings with consumer reporting agencies, complaint counsel rely on three extracts from Capax dunning letters (See CPF # 58):

> PAID IN FULL WITHIN SEVEN DAYS, THIS ACCOUNT WILL NOT BE SHOWN ON OUR CREDIT RECORDS. . . . FORWARD YOUR PAYMENT NOW DIRECTLY TO A-B-C- SUPPLY COMPANY IN ORDER TO RECEIVE PROPER CREDIT. . . (first contact), Diplomatic series, CX 10(b)-(c); CX 17(b); Spanish series, CX 12(b)-(c); CX 19(b);
>
> UP TO NOW YOUR CREDIT STANDING WITH A-B-C- SUPPLY COMPANY HAS BEEN SATISFACTORY. CREDIT IS A PRIVILEGE, NOT A RIGHT. IT IS IMPORTANT TO PROTECT THIS PRIVILEGE, BECAUSE ONCE IT IS LOST IT IS ALMOST IMPOSSIBLE TO REPLACE. LIKE MOST OTHER PRIVILEGES, YOU ONLY MISS IT WHEN YOU NEED IT. (third contact, Diplomatic series, fifth contact, Diplomatic series, second contact, Bad check series), respectively, CX 10(e); CX 17(f); CX 21(c); Spanish series, CX 12(g); CX 19(f);
>
> . . . YOUR CREDIT STANDING MAY SUFFER. . . (fourth contact), Strong series, CX 11(f)-(g); CX 18(e); Spanish series, CX 13(g); CX 20(e);

51. None of these extracts makes any reference to consumer

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[15] Vineburgh, $989.06 (CX 47); Gordon, $467.50 (CX 48); Zuccarrelli, $354.18 (CX 44); $135.00 (CX 46); Gardner, $129.30 (CX 29(d)0.

[16] Gravatt, $8.32 (CX 342); Cook, $19.95 (CX 58); Nield, $25.27 (CX 51); Thom, $38.00 (CX 45).

reporting agencies or the credit ratings they dispense. Moreover, the first letter [CX 10(b) et al.] expressly refers to the debtor's account not yet shown on *Capax' own credit records.* The second letter [CX 10(e) et al.] expressly refers to the debtor's credit standing with the *particular creditor involved.* Moreover, subsequent reference therein to **[40]** the importance of not losing the privilege of credit plainly relates back to the debtor's credit standing with this particular debtor. As for the third letter [CX 11(f) et al.], reference to the full paragraph of which it is a part[17] reveals that the situation contemplated is an adverse effect on the debtor's credit standing *incidental to a lawsuit.*

52. The first two examples plainly do not relate to the debtor's *general* credit standing and the third, which *may* be read to relate to the debtor's general credit standing (Tr. 595–596), nevertheless does not threaten an active effort to affect the debtor's credit adversely. It is only a proper reminder that, *if* a lawsuit be brought — as is clearly any creditor's right — one of the *incidental* results may be — as clearly it may — that the debtors' credit rating *may* suffer. We find that proof of such a warning has no logical tendency to support the allegation of Complaint Par 8.3 that Capax threatened to adversely affect debtors' credit ratings with consumer reporting agencies.

53. Complaint counsel's further contention that 4 of the 9 debtor witnesses presented by complaint counsel were led to believe their credit records would be adversely affected if they did not pay up is not supported by the evidence. Whether these 4 witnesses even weighed the warning in the balance is really quite unsure because none of them paid up. Two promptly hired lawyers for a good fight on the merits of their disputes with the creditors involved. (Gardner, Tr. 282, 295; Gordon, Tr. 377) A third, an experienced bill collector, always doubted that she would really be sued for $19.95 (Tr. 516–A). The **[41]** fourth was assured from the start by her creditor that Capax had made a mistake which she could disregard. (Cook, Tr. 492, 496) Since the whole point of deception evidence is to prove a tendency to deceive, debtors who were not *really* deceived add nothing to the proof of a *tendency* to deceive.

54. Even, however, if all of them had taken Capax' warning to heart — to the exclusion of all other considerations — and had all immediately paid the debts in question, it is hard to see any deception in Capax' persuading them to do so by reciting such a simple truth as that a credit rating *may* suffer *if* a lawsuit has to be brought to collect a debt. Accordingly, we find that even if the warning proved had

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[17] "If this (i.e. a satisfactory arrangement for payment) is not done, [Capax] can take no other position but to recommend a stronger course of action to our client. . . If this is done there may be additional costs to you and your credit standing may suffer."

corresponded more closely to the warning *pleaded*, and even if such warning had had some effect on these debtors' *actions*, there was no tendency for the simple truth stated in these letters to deceive anyone.

Threats To Enforce Prompt Payment

55. In proof of complaint Pars. 8.4 and 9.4, which allege that respondents have falsely represented the immediacy of action, such as suit, to be taken to collect a debt, unless payment be received within a time specified by respondents. Complaint counsel direct our attention to thirteen extracts from Capax' dunning letters (CPF # 60).

56. However, most of these extracts are not relevant to complaint Pars. 8.4 and 9.4. They are simple demands to pay an already overdue debt within a specified time such as "48 hours" [*e.g.* CX 10(m)] or "five days" [*e.g.* CX 10(l)] or "at once" [*e.g.* CX 11(f)] without specifying what would happen if the debtor did not pay within the specified time. The purpose, as Capax' President testified, was simply to fix "a time frame" to get the debtor "off his rump" (Tr. 605–5) and pay up as quickly as possible (Tr. 535). The debtor may or may not meet the demand but the demand, by its very nature, is not a representation capable of being found true or false. Significantly none of complaint counsel's debtor witnesses alleged [42] deception by any of the eight sanctionless demands irrelevantly included in CPF # 60. Accordingly, we now limit our consideration to those 6 of the extracts cited in CPF # 60 which warn the debtor that some sanction, such as suit, will be invoked against him if he does not meet a specific new deadline.

57. The extract of this kind most commonly testified to by debtor witnesses here (Thom, Tr. 128; Gordon, Tr. 355; and Zuccarrelli, Tr. 661–2), reads as follows:

> **If not paid within one week, to liquidate this matter we will be forced to recommend action which may mean added costs to you. . . Prompt action in this matter is imperative. Make immediate payment directly to [the creditor]. . . [See CX 11(c); CX 18(b) and CX 62(a), *inter alia*]**

58. Debtor witness Zuccarrelli, apparently attaching no significance to the word "recommend" testified simply: "Well, from the letter I thought it (suit) would be instituted immediately." (Tr. 662) It does not appear, however, that she was sufficiently concerned to pay the bill. A second recipient (Thom) agreed that "suit" is nowhere mentioned in this letter but thought the statement that "we will be forced to recommend action" was "imperative." (Tr. 128) Nevertheless, she, too, apparently never paid the bill for which Capax dunned her. The third recipient, Gordon, was left unsure about what action was going to be taken but suspected an intention to take action against his

credit — how soon, however, he did not testify. (Tr. 355) In any event he apparently never paid the bill.

59. Another debtor witness (Gravatt, Tr. 311) received a different extract:

> . . . If you do not correct this matter quickly, we will have to recommend that our client exercise all legal means to recover the loss. [CX 14(b)] [43]

Although this includes no definite deadline and, like the others, speaks only of a recommendation, not a suit, young Ms. Gravatt testified that on receipt of this letter in TELEGRAM format "all I thought was really soon, very soon afterwards." (Tr. 311) Her mother quickly made good the bad check in question at the young witness' request. (Tr. 325)

60. Another debtor witness (Viera, Tr. 492–6) received a Spanish language dunning letter [CX 12(c)], an extract from which she translated as follows:

> Pay this account completely within 7 days. This account won't show or appear in your[18] credit register.

Ms. Viera recited this language as explaining her concern about possible injury to her credit record[19] but no mention was made of any reaction to the "7 days" language. (Tr. 492–496) In any event, she was not led to make payment.

61. The last of the 6 debtor witnesses who are cited in CPF # 61 [Gardner, Tr. 250–252] received the CX 29 series of dunning letters, one of which [CX 29(o)] is cited in this connection by complaint counsel. CX 29(o), the next to the last of the series, was stamped "NOTICE" and contained the following extract:

> If you want to avoid unpleasant and costly action, make immediate payment. . . . We can wait no more than 5 days to hear from [the creditor] on settlement. Your immediate response is imperative. [CX 29(o)] [44]

62. The last of the series [CX 29(q)] was stamped "FINAL NOTICE" and contained the following extract:

> You may immediately register your defense in writing within 48 hours after receipt of this notice. [CX 29(q)]

According to Gardner's own testimony it was the stamp "FINAL NOTICE" on the last letter [CX 29(q)] — rather than the deadline set in CX 29(o) — which led Gardner to "assume that it (suit) would happen some time in the immediate future." (Tr. 263)

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[18] Although not corrected during the witness' examination, reference to a Spanish-English dictionary indicates either that Ms. Viera erroneously translated "su" to mean "your" instead of "our" or that the report of the testimony is wrong. 494–5.

[19] Obviously a proper translation would have much lessened even this concern.

63. In summary, of the nine debtor witnesses selected from some 2000 candidates, only six are cited on this point. Of the six only three (Zuccarrelli, Viera and Gravatt) claimed to have been led to believe suit was imminent and of those three debtor witnesses only one (Gravatt) was, in fact, sufficiently concerned to pay the debt (or, in her case, to have her mother pay it.)[20] The claim of one young girl to have taken Capax' warnings of immediate action seriously enough to act on them is too slender a reed on which to find that such warnings had a real capacity to deceive the ordinary debtors who received them.

64. We find, rather, that these traditional warnings by creditors or their agents to debtors were recognized as mere bluff or bluster, analogous to "puffing" in merchandising. As Capax' President [45] testified, the failure of a debtor to meet a Capax deadline would normally result only in his getting the next letter of the series [Tr. 562, 579]. The debtor here — like debtors generally — learn that such threats are commonly harmless and may commonly be disregarded — for a long time, at least — with impunity.

65. The evidence here shows clearly how this comes about. Take as an example witness Gardner (drama critic for the Baltimore Sunpapers), who received the CX 29 dunning series. The sequence of this series is as follows. The first [CX 29(d)], dated 1/10/75, tells the debtor that he can keep this claim out of Capax' credit records by settling the account in question within 7 days. The next [CX 29(h)] dated 1/27/75 (or more than 2 weeks later) suggests an "oversight" and advises that payment will still be accepted. The next [CX 29(f)], dated 2/5/75 warns that "little time remains" but "the worst" can still be avoided by reaching an arrangement with the creditor. The next [CX 29(i)], dated 2/19/75, warns that "strong action" is often necessary but "there is still time to avoid the unnecessary consequences of your neglect."

66. The next [CX 29(k)], dated 2/28/75 lays down the law: "It is imperative that you contact your creditor *today* to avoid further action." (emphasis added). Yet two weeks later, on 3/14/75, comes another [CX 29(m)], again asserting that it is "urgent" and "imperative" that satisfactory arrangements be made and "if settlement is not made *within 48 hours* upon receipt of this LETEGRAM, we suggest you contact your attorney to determine your legal liability. . ." (emphasis added) A week later the dunning starts again. On 3/21/75 CX 29(o) (stamped "NOTICE") warns that it would be "most unfortunate" to

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[20] While young Ms. Gravatt was married by the time of trial she had been living with her parents and attending school in Washington, D.C. in 1973, when the incident occurred. (Tr. 308) She had never received a telegram (Tr. 317) and had never been dunned for a debt (Tr. 320–1). She did not bother to maintain a record of her checks as written (Tr. 344) and had not bothered to look at her monthly bank balance after giving Sears, Roebuck a bad check for $12 (Tr. 334) which was the basis for the dunning letter. As respects financial matters she could hardly be called an ordinary debtor.

make "more formal action" necessary and lays it on the line: "We can wait no more than *5 days* to hear. . . Your immediate response is imperative." (emphasis added) Nearly two weeks later, on 4/2/75 Capax sends a "FINAL NOTICE" which gives witness Gardner "*48 hours* after receipt of this notice" to "register" his **[46]** defense, etc. (emphasis added) — but payment will still be accepted, not too surprisingly. [CX 29(q)] Then follows a six months breathing spell, after which, on 10/3/75 a new series starts all over again: "This is your final opportunity. . . ."

67. A review of each series of Capax' dunning letters *in their entirety* convinces us the deadlines and exhortations to urgency found in such letters do *not* convey to the debtor the same serious message that each letter viewed individually might convey to an uninvolved reader. Indeed, it is hard to believe that an ordinary debtor will take a creditor's "5 days-to-pay," "48 hours to pay," "pay at once," etc. any more seriously than a merchandise buyer takes a hawker's "Hurry, hurry, hurry. . . while they last. . ." Sooner or later the constant dunning may stimulate the debtor to begin payment sometime during the series but it seems doubtful that the setting of deadlines plays any significant role in the process, as the almost total ineffectiveness of such "warnings" clearly confirms.

68. We find that Capax' warnings of immediate sanctions if its payment deadlines are not met may be "false" in a literal sense, because Capax is plainly programmed to give the debtor a second chance, third chance, fourth chance, etc., if payment is not made within the stated time. However, we also find that the ordinary debtor would recognize from the repetitive pattern of inconsistent warnings and forgiveness — even if he has not, like most debtors, had similar experience with other dunning agencies — that Capax' exhortations to urgency may be taken with a grain of salt. Like merchants' puffery they lack the capacity to deceive which is the ultimate issue here. They are mere bluff and bluster. **[47]**

CONCLUSIONS OF LAW

1. The Federal Trade Commission has jurisdiction over the subject matter of this proceeding and personal jurisdiction over all respondents.

> *Comment:* Jurisdiction over the subject matter here is found in Section 5(a) of the Federal Trade Commission Act, 15 U.S.C. 45(a). Jurisdiction over the person was obtained by service of the complaint on all respondents and the subsequent general appearance of each respondent by attorney. See page 8 above.

2. The acts and practices charged in the complaint and proved here took place in commerce, within the meaning of the Federal Trade Commission Act, 15 U.S.C. 45(a).

> *Comment:* All respondents concede this and there is no question of collusory jurisdiction. See Findings # 12 thru 15 above.

3. All individual respondents concede that as long as they were active in the affairs of this close corporation they did (and respondent Goodman still does) formulate, direct and control its acts and practices generally. Respondents Goodman and DeFelice further concede that they have formulated, directed and controlled the particular acts and practices which are the subject of this complaint. Respondent DeFelice denies but we now find that he, too, participated personally in various acts and practices which are the subject of this complaint.

> *Comment:* See Findings # 1 thru 5 above. For a holding that domination of corporate affairs generally is sufficient to hold an individual, see *Tractor Training Service, Inc.* v. *F.T.C.*, 227 F.2d 420 (9th Cir., 1955). For a holding that [48] there must be a further showing that such individual actually participated in the challenged acts and practices. *Coro, Inc., et al.* v. *F.T.C.*, 338 F.2d 149, 154 (1st Cir., 1964) *(cert. den.,* 380 U.S. 954). We find both tests met here with respect to all individual respondents, including Bricker.

4. The acts and practices of respondents proved in this proceeding do not constitute unfair or deceptive acts or practices in commerce and are therefore not violative of Section 5(a) of the Federal Trade Commission Act, 15 U.S.C. 45(a).

> *Comment:* This is primarily a factual case and our resolution of factual issues is already apparent from our findings. It remains only to note the major legal assumptions behind our findings of fact.

A. LETEGRAM

We have found as a fact that the purplish red and gray LETEGRAM format used by Capax since the fall of 1973 is not likely to deceive the ordinary debtor into believing it is really a telegram and not likely to deceive any debtor more than momentarily, certainly not long enough to affect any decision. (Findings # 18–22). While it is clear that the unfair trade practice law is designed to protect the "ordinary purchaser" rather than the common law's "reasonable man", *F.T.C.* v. *Sterling Drug, Inc.*, 317 F.2d 669, 674 (2d Cir., 1963) and there is also talk in our cases about protecting "the gullible and credulous" as well as "the cautious and knowledgeable," *Charles of the Ritz* v. *F.T.C.*, 143 F.2d 676 (2d Cir., 1944), nevertheless ". . . . a representation does not become 'false and deceptive' merely because it will be unreasonably misunderstood by an insignificant and unrepresentative segment of the class of persons to whom the representation is addressed." *Kirchner t/a Universe Co.*, 63 F.T.C. 1282, 1290 (1963). [49]

Here our finding is based not only on our own visual inspection of CX 17(b) but on the adverse inference which we are permitted to draw from complaint counsel's failure to ask 6 of their 9 debtor witnesses whether they really mistook a LETEGRAM for a TELEGRAM; the fact that one of the remainder was testifying about a TELEGRAM instead of a LETEGRAM; and the atypical nature of the other two debtor witnesses, one of whom, incidentally did not assert more than initial confusion.[18]

While these matters are not to be decided by a Gallup Poll, the top-heavy support for our conclusion that a LETEGRAM is readily recognizable as a gimmick, not a TELEGRAM, is not to be defeated merely because for a moment a LETEGRAM may be "unreasonably misunderstood by an insignificant and unrepresentative segment" of debtors.

B. "COLLECTION AGENCY" IMAGE

This case was apparently premised on an erroneous theory of law that there is something *per se* deceptive about a debtor-dunning service which does not include all other collection functions as well as dunning. Put simply, Capax' short-line debt collection service (largely just dunning letters) is viewed as inherently [50] deceptive because, by definition, it is not a full-line service (which would apparently have to include such things as regularly receiving payments and bringing suits, as needed). According to Paragraphs 8.1 and 9.1 of the complaint the very use of the word "collection" in Capax' letterhead[19] constituted a misrepresentation that:

> delinquent debtors' accounts have been referred to respondents as an independent debt collection agency which will engage in typical debt collection activities such as making personal demands for payment and/or filing suit.

Authority for this position is said to derive from the language of Commissioner Jones in *State Credit Control Board*, 70 F.T.C. 1318 (1966); *affd. sub nom. S. Dean Slough* v. *F.T.C.*, 396 F.2d 870 (5th Cir.,

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[18] We recognize the rule of *Carter Products, Inc.* v. *F.T.C.*, 186 F.2d 821, 824 (7th Cir., 1951) that even correction of an original misapprehension before action in reliance, as by entering into a contract, may not cure a violation. However, in this case we have found no more than a possible momentary deception, which would be immediately recognizable as an error. This is a horse of a different color (purplish red and gray, of course).

[19] Capax' messages other than "Letegrams" were commonly headed: "Continental Credit Corp . . . . Credit Control and Collection."

1968); *cert. den.*, 393 U.S. 980 (1968). That case was primarily concerned with a different problem: stopping the misleading use of a false aura of governmental authority by a private dunning service. With that holding of the case it would be hard to disagree.

However, Commissioner Jones also held (without regard to emulation of governmental authority) that mere use of a third party dunning agent in the circumstances of that case was deceptive:

> Third party referral, to the extent it is an effective debt-collection device, is effective because it implies to the debtor that the third party has collection authority or authority to take other legal action. If the third party does not in fact have such authority the mere lending of its name and address to the collection of the debt is wholly grounded in deception (p. 1358) (emphasis added) [51]

And again:

> The record demonstrated that use of third-party referrals is important in the collection of delinquent accounts. The evidence clearly indicates that third party referrals have this significance not simply because debtors are more apt to read what is sent by third parties,[20] but more importantly because of the debtor's assumption from the fact of such referral that the creditor has placed the delinquent account in the hands of a third party for some affirmative action (transcript citations). Debtors receiving any third-party communications respecting their delinquent accounts are thereby led to believe that their creditors will no longer extend credit and that they probably intend to collect the debt by legal action if necessary. (p. 1357)

If Commissioner Jones' opinion means that any third party referral of a debt which does not confer full authority to receive payment, bring suit, etc. is *per se* deceptive and unfair, there would be no point in pursuing this matter further: indeed, the whole dunning business would be unlawful. We are reasonably sure that *State Credit Control Board* was never intended to abolish the debt dunning business. There are several references in Commissioner Jones' opinion to record sources, such as the respondent's exposition of so-called "third party" psychology, as the basis for her conclusion in *that* situation and under *those* circumstances. Accordingly, we have assumed that it will not be *presumed* but must be *proven* in every case that a referral was made in such a way and under such circumstances as to create a likelihood or fair probability that debtors receiving dunning letters will be deceived to their prejudice. [52]

In Findings 29–38 we have found from the testimony of complaint counsel's own debtor witnesses that they did not, in reality, act the way that complaint counsel's theories presume they should act. It was *not* mere notice that a claim had been turned over to Capax which led most of these debtor witnesses to anticipate that they would be sued or their credit would be ruined, etc. With no more than one or two possible exceptions, these debtor witnesses all attributed their alleged fears about suit or credit standing to specific language other than a mere announcement that the debt had been turned over to Capax for its action. Such findings confirm our reading of *State* to call for a realistic appraisal of the evidence in each case, not a wooden reliance of an unrealistic presumption which, if rigidly applied, would put the dunning business out of business.

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[20] Respondent had expressly conceded this proposition (pp. 1353–1354).

C. THREATS OF SUIT

We have concluded in Finding # 45 that alleged threats of suit in Capax' dunning letters would not deceive an ordinary debtor into believing he was going to be sued by Capax, because most such letters made it quite clear on their face that any suit would be by the creditor (and none were contra). To reach our conclusion it was necessary to disregard contrary testimony by some of complaint counsel's debtor witnesses but that results in no weakness in our conclusion. As the Courts have held, the Commission is not bound in a matter of this kind by statements of witnesses as to whether they were deceived or not. *Double Eagle Lubricants, Inc.* v. *F.T.C.*, 360 F.2d 268, 270 (10th Cir., 1965). In this case the documentary evidence is all one way. It would be a travesty on justice to believe the contrary testimony of the debtor witnesses.

The ultimate issue on this branch of the case is whether it is deceptive for Capax in some instances to warn debtors that their creditors will sue them, without making specific inquiries of the specific creditors involved, on the basis of Capax' extensive experience with creditors and debtors generally and this creditor in particular. The Commission case law [53] in such situations does not require Capax to be an insurer of the accuracy of its warning but only to have a reasonable basis for its statement. *Pfizer, Inc.*, 81 F.T.C. 23 (1972); *Tashof* v. *F.T.C.*, 437 F.2d 707 (D.C. Cir., 1970). The extensive background for Capax' warnings, set forth in part in Finding # 47, leaves no question about what would seem highly probable anyway: that creditors almost always bring suit, assuming economic feasibility, for debts that the dunner leaves uncollected.

D. THREATS TO CREDIT STANDING

On this branch complaint counsel's showing is so deficient on the facts that there is little occasion to apply law. Two extracts from complaint counsel's three alleged examples reveal only unexceptionable warnings that the debtor's credit with Capax and/or the creditor may suffer if he doesn't pay the debt. The third could be read to refer to the debtor's general credit reputation but, again, merely reminds him that if the claim goes to trial "your credit standing may suffer."

It is hard to see how dunning could survive if a dunner could not argue such a simple truism as this. There may be occasions when truth is presented deceptively but that is certainly not the case here; a truer warning can not be imagined. The warning may be *unpleasant* but that is no proper concern of this Commission. As the Commission stated when it was starting down the road of policing deception in debt collection:

> . . .(A)ll persons should pay their just debts. Within legal limits, creditors are entitled to pursue their collection methods energetically. *Wm. H. Wise Co., Inc.*, 53 F.T.C. 408, 426 (1956)

It is important to remember that the purpose of the Commission's activity in this field is to prevent deception, not to prevent energetic collection methods. [54]

E. THREATS TO ENFORCE PROMPT PAYMENT

The last legal issue in this case concerns Capax' occasional[21] setting of early time limits within which debtors are warned to pay up or face the prospect of defending themselves in court or other unpleasant consequence. There is no doubt but that Capax has set such deadlines and yet has regularly given debtors second, third, fourth and more chances to meet new deadlines while the series of dunning letters drags on. The legal issue is not whether the use of a *locus penitentiae* — known to and employed by every lawyer in this country — is fair or unfair in other ways but whether it has a tendency or capacity to deceive — to put it simply: whether anybody really takes those deadlines seriously.

"Puffing" is one of the few defenses from the common law of misrepresentations which has survived into the law of deceptive trade practices, as evolved and administered by this Commission, Kintner, E.W., *A Primer On The Law Of Deceptive Practices* (1971), pp. 7–8, 33, albeit with some restrictions, *e.g. ibid.* p. 319, *et seq.* The "puffing" rule gives merchants some freedom to describe their wares in enthusiastic terms which most people would readily recognize to be exaggerated. See, for example, *H. W. Kirchner, t/a Universe Co.*, 63 F.T.C. 1282 (1963). There the Commission recognized the possibility of a technical violation of the unfair trade practice law when a respondent advertised as "invisible" a "Swim-Ezy" flotation device worn under a bathing suit which was, in fact, no more than "inconspicuous":

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[21] Most of Capax' deadlines, it will be remembered, specified no sanction for failure to perform in time. Such demands are not susceptible to misrepresentation.

> To be sure, "Swim-Ezy" is not invisible or impalpable or dimensionless, and to anyone who so understood the representation, it would be false. (p. 1289) [55]

Nevertheless, Commissioner Elman continued:

> It is not likely, however, that many prospective purchasers would take the representation thus in its literal sense. (pp. 1289–90)

And the Commission thereupon dismissed that part of the charge (p. 1291).

What puffery is to a merchant, bluff and bluster are to a debt dunner. "Time frames" come naturally to a dunner in order to get debtors "off their rumps," as Mr. Goodman, Capax' President, put it here (Tr. 604–5). But it is "not likely," to use Commissioner Elman's words, that "many" debtors take those time frames seriously. We are satisfied that an "ordinary"[22] debtor would "probably" react in about the same way we do to the continuing parade of ever-new deadlines illustrated in Findings # 65–66 above. That they will not be taken seriously by most debtors is clearly confirmed here by the single instance of success for such methods among complaint counsel's nine debtor witnesses. Such bluff and bluster by debt dunners has no more real capacity to deceive than the merchant's traditional puffery. It would be a serious mistake to treat such warnings with the seriousness reserved for representations with a real capacity to deceive.

5. On consideration of the whole record, including only the reliable, probative and substantial evidence therein contained, it is the initial decision of the administrative law judge, pursuant to the [56] provisions of this Commission's Rule Section 3.51, that the complaint in Matter of Capax, Inc., Dkt. 9058, should be and hereby is DISMISSED.

OPINION OF THE COMMISSION

BY DOLE, *Commissioner*

This matter is before the Commission on an appeal by complaint counsel from an initial decision of the administrative law judge dismissing the complaint. The complaint charged that respondents Capax, Inc., two present officers, and one former officer had violated Section 5 of the Federal Trade Commission Act by making false and misleading representations in form notices and letters sent to debtors to assist in the collection of alleged delinquent debts. After an evidentiary hearing, Administrative Law Judge (ALJ) Paul R. Teetor issued his initial decision, which concluded that respondents' practices are neither deceptive nor unfair and therefore do not violate Section 5. [2]

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[22] That the test is the "probable" reaction of an "ordinary" person, see again *F.T.C. v. Sterling Drug, Inc.*, 317 F.2d 669, 674 (1963).

Upon our review of the record, the arguments advanced in the briefs and at oral argument, and the initial decision, we reverse. The ALJ's order dismissing the complaint and his findings of fact and conclusions of law are vacated, and the findings and conclusions set forth in this opinion are substituted in their place, except to the extent that the ALJ's introductory findings of fact[1] are not inconsistent with this opinion.

BACKGROUND

Since its inception in 1972, respondent Capax, Inc. ("Capax") has been engaged in selling a service to assist creditors in various parts of the United States in the collection of alleged delinquent debts. (I.D. 6, 12–15.)[2] Respondents DeFelice, Goodman, and Bricker are present or former officers and principal owners, all of whom were properly found by the ALJ to have formulated, directed, and controlled the acts and practices of Capax. (I.D. 2–5.) Capax' service has consisted primarily of the preparation and mailing of a series of form letters, purchased by creditors at a flat rate and sent by Capax at regular intervals to alleged delinquent debtors. The service is provided on a non-commissioned basis. (I.D. 6.) [3]

Capax' clients can choose between several different series of dunning letters. There are long and short versions of a "strong" series,[3] a "diplomatic" series, a "bad check" series, and various Spanish language series. The charge for the long series was about $3.84 when the business was formed and later was increased to $4.25 (I.D. 7); it includes the mailing of a maximum of eleven letters (Tr. 795) over a period of approximately 90 days. (Tr. 801; CX 24(b), RX 91.) The short series consists of fewer letters sent out over a shorter period of time,

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[1] I.D. 1–15.

The following abbreviations are used in this opinion:

I.D.	— Initial Decision (Finding No.);
I.D. p.	— Initial Decision (Page No);
Tr.	— Transcript of Testimony;
CX	— Commission Exhibit;
RX	— Respondents' Exhibit;
App. Br.	— Complaint Counsel's Appeal Brief;
Ans. Br.	— Respondents' Answering Brief;
Rep. Br.	— Complaint Counsel's Reply Brief;
TROA	— Transcript of Oral Argument before Commission.

[2] Capax was named Continental Credit Corp. until January 21, 1975. (I.D. 1.)

[3] This was formerly called the "deadbeat" series. (Tr. 776–777; TROA 57).

and is available to creditors with a high volume of low-balance accounts. (Tr. 883.)

Capax has promoted itself as a "customized, computerized control company" which is "not a collection agency" and which offers "the modern answer to an old problem."[4] According [4] to Capax' President, Mr. Goodman, the company's dunning letter service is part of a more comprehensive "credit control system consisting of sending out the letters, generating reports and advice and helping to control the receivables for the individual company." (Tr. 504, *et seq.*). In fact, the company's service operates in a rather simple and mechanical manner: a creditor who purchases the flat rate service is provided with several transmittal forms which are used to start the service (CX 33; CX 27; Goodman, Tr. 520–521, 526, 528); to suspend it if payment is received or satisfactory arrangements are made (CX 27; Goodman, Tr. 752–758); and to resume it under certain circumstances.[5] Capax' letters advise debtors to make payment directly to their creditors; money

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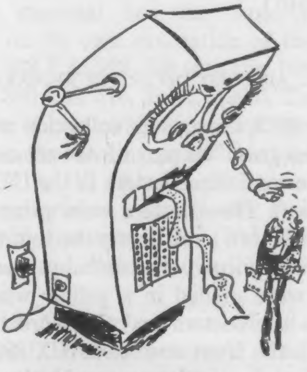
[4] CX 9(a). This exhibit, a promotional circular, provides the following illustration:



THE MODERN ANSWER

To An Old Problem

[5] The service is resumed if the debtor fails to make a satisfactory payment or if Capax has temporarily suspended the service after contact by a debtor disputing the claim and the creditor requests that it be continued. (CX 27; Goodman, Tr. 758–759, 687–688.)

which is sent to Capax is immediately forwarded to the creditor. (I.D. 9.)[6]

When the flat rate letter writing service fails to result in payment of a debt, Capax advises the creditor of stronger actions which could be taken. (I.D. 8.) Since about May 1975, Capax' clients have been offered a "second phase" collection service for "hard core cases" where the flat rate letter writing service has not induced collection of a debt. (I.D. 10.) Capax' President testified that in "Phase 2" phone calls may be made to the debtor (Tr. 553, 791–792).[7] [5] Capax charges a fee for this supplementary service based on a percentage of the debt collected. (Tr. 796.)[8]

Capax has never had contractual authority from its clients to bring suit against debtors, either in its own or the creditor's name, nor has it ever brought such a suit. (I.D. 11.) In its flat rate service, Capax does not take assignments of the debts referred to it (I.D. 6; Tr. 824; CX 7(a)), and has no knowledge during the course of its letter writing series whether the creditor would take collection action if payment was not received. (Tr. 543, 567, 587–590, 600–601.) Likewise, in conducting its flat rate service, Capax has taken no action to adversely affect the debtor's credit record with a consumer reporting agency (CX 60(o), CX 61(i); Tr. 231, 537–539) and has had no control over or knowledge of whether a creditor would take any such action, if payment was not received. (Tr. 532, 546.)

I. ALLEGED DECEPTIVE APPEARANCE

Prior to October 1973, Capax sent collection notices to debtors which were captioned "Telegram" as part of its various dunning letter series. (*See* the initial letter and other letters in the CX 17, CX 18, CX 19, CX 20, and CX 21 series). These letters were printed with large type on yellow paper with a brown band across the top; the notations "DAYTIME MESSAGE URGENT" and "NIGHT MESSAGE" appeared adjacent to selection boxes. The forms were mailed in a yellow window envelope with a brown band across the bottom and the word "Telegram" appearing three times on both the front and back. (CX 22(b).) Although none of these were actually telegraphic communications (CX 60(r), 61(j); Tr.

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[6] Between October 18, 1973, and October 10, 1974, payments amounting to approximately $20,000 were sent by debtors to Capax. (CX 60(r), CX 61(i); Tr. 241.) According to the testimony of Capax' President, this represented about 2 percent of the $10 million worth of claims collected for clients during this period, which in turn represented 51 percent of the $20 million of claims submitted by creditors to Capax for its service. (Tr. 881–883).

[7] The ALJ made the finding that in Phase 2 the claim may be turned over to an attorney for suit, unless the creditor gives Capax specific orders to the contrary. (I.D. 10.) Actually, Mr. Goodman testified that in the second phase a recommendation may be made by Capax to refer the account to an attorney for further action. (Tr. 555, 802.) This does not appear to represent a change from Capax' pre-Phase 2 operations.

[8] Phase 2 was initiated after Capax had been informed of the Commission's investigation. (CX 1(a).)

240), they bore a close resemblance to Western Union telegrams (*See, e.g.*, RX 27(a), RX 27(b)).

In October 1973, Capax discontinued its use of the "Telegram" format,[9] and since that time has used a "Letegram" format. (*See* the initial letter and other letters in the CX 10, CX 11, CX 12, CX 13, CX 14, CX 15, and CX 16 **[6]** series; CX 60(q) and CX 61(i); *see also* CX 22(c), which is a sample "Letegram" envelope.) The "Letegram" is printed in the same type style as its predecessor, but on gray paper with a magenta band across the top. The caption "Letegram" appears in the band, with the words "URGENT MESSAGE" in the center of the band. The "Letegrams" are sent in gray window envelopes with a magenta band across the bottom and the word "Letegram" appearing three times on both sides of the envelope. Like the "Telegrams" respondents formerly used, the "Letegrams" are not actually telegraphic communications, but are letters sent by United States mail. (CX 60(q), CX 61(j).)

The complaint alleged that these materials simulate telegraphic or similarly urgent communications and thereby mislead recipients as to their nature, import, purpose, and urgency. It is well established that tendency or capacity to deceive, as well as actual deception, falls within the proscription of the FTC Act. *FTC* v. *Sterling Drug, Inc.*, 317 F.2d 669, 674 (2d Cir. 1963); *Regina Corp.* v. *FTC*, 322 F.2d 765, 768 (3rd Cir. 1963); *Goodman* v. *FTC*, 244 F.2d 584, 604 (9th Cir. 1957). In determining whether material has the capacity to deceive, the Commission may rely on its own evaluation of the evidence, *Carter Products, Inc.* v. *FTC*, 323 F.2d 523, 528 (5th Cir. 1963); *see also FTC* v. *Colgate Palmolive Co.*, 380 U.S. 374, 391–2 (1965). The Commission may interpret the meanings of communications and the "impressions they would likely make upon the viewing public," *Libby-Owens-Ford Glass Co.* v. *FTC*, 352 F.2d 415, 417 (6th Cir. 1968), and may look to the overall impact of the material at issue. *Carter Products, Inc.* v. *FTC*, *supra*. *See Trans World Accounts*, F.T.C. Dkt. 9059, at 3–6 (Oct. 25, 1977) [90 F.T.C. 350], *appeal docketed*, No. 78–1398 (9th Cir. Feb. 21, 1978).

Turning first to the "Letegram," our visual inspection of the "Letegram" letters and envelopes reveals that they sufficiently resemble genuine telegraphic communications to have the tendency and capacity to deceive recipients as to their nature, import, and urgency.[10] Although the simulation of a telegraphic communication is less blatant [7] as to the "Letegram" than the earlier "Telegram," the overall appearance of the "Letegram" has the capacity to deceive consumers into believing that it is more urgent and significant than an ordinary letter. Both the name "Letegram" and the format of the communication are susceptible of being confused by members of the public with a telegraphic communication.[11] With respect to respondents' earlier "Telegram" format, we agree with the ALJ that there is little doubt that the "Telegram" was virtually indistinguishable from a real telegram—it had the same colors, size, and shape, and similar type.[12] As a result of respondents' simulated telegraphic [8] formats, especially in conjunction with the messages employed, discussed *infra*, the recipient is led to believe that the creditor considers the message so urgent that he went to the trouble and expense of using a telegraphic communication. "The obvious conclusion to be drawn from the receipt of a demand to pay, telegraphically communicated at substantial cost, is that precipitous action may follow if immediate response to the message is not made." *Trans World Accounts*, *supra* at 4.

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[9] However, there may have been some exceptions. One witness, Ms. Gravatt, testified that she received the yellow "Telegram" (CX 21(b)) from Capax in early 1974 (Tr. 310–311, 326), after the date that respondents represent the telegram format was abandoned.

[10] We do not find, however, that the simulation misleads recipients of the "Letegram's" purpose, as the complaint had charged.

The testimony of complaint counsel's witnesses corroborates our view. Ms. Nield testified: "My initial impression upon receiving [the "Letegram"] was that it was a fairly urgent message. It appeared to be a telegram or a Western Union letter, or gram or whatever." (Tr. 148–149.)[13] Her impression was based upon "the format, the letter, the envelope, the letterhead, the style of print." (Tr. 149). On cross-examination, she reiterated that her impression upon receiving the "Letegram" was that it was an urgent, telegraphic [9] communication. (Tr. 158-159.) Ms. Cook testified that when she received Capax' first

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[11] We note that although Capax' "gram" is no longer the same color as a Western Union telegram, not all authentic telegraphic communications are yellow and brown. For example, the Western Union Mailgram, a message telegraphically communicated to the general locale of the recipient and mailed from there, is blue and white. (RX 28, 29(a), RX 29(b), RX 30(b).)

[12] Respondents content (Ans. Br. 14) and the ALJ found (I.D. 16) that use of the "Telegram" was abandoned in October 1973. This was prior to the preliminary inquiry letter to Capax, notifying it of a Commission investigation. (CX 1(a), dated January 31, 1974). Although there was some testimony that the "Telegram" format may not have actually been abandoned before initiation of the investigation, *see* n. 9 *supra*, the weight of the evidence is that Capax did generally abandon that format, as claimed.

Contrary to the ALJ's ruling that the complaint made no charge of deception with respect to the "Telegram," the allegations of the complaint were sufficiently broad to encompass the "Telegram." Paragraph Four of the complaint referred to "various printed forms, letters, and other printed material," with reference to the "Letegram" as "(t)ypical and illustrative, but not necessarily all inclusive of said forms and material."

Whether a claim of discontinuance of early deception is to be accepted is within the discretion of the Commission, *Benrus Watch Co.* v. *FTC*, 352 F.2d 313, 322 (8th Cir. 1965), *cert. denied*, 384 U.S. 939 (1969); *Libby-Owens-Ford Glass Co.* v. *FTC*, 352 F.2d 415, 418 (6th Cir. 1965). Under the circumstances here, where abandonment of a form of deception was followed by another form of deception, less blatant but still unlawful, we reject the abandonment defense. Discontinuance of an offending practice, particularly under circumstances where there is no assurance that the deception will not be resumed, does not obviate the need for or propriety of an order. *Cotherman* v. *FTC*, 417 F.2d 587 (5th Cir. 1969); *Libby-Owens-Ford Glass Co.* v. *FTC*, *supra; Coro, Inc.* v. *FTC*, 338 F.2d 149 (1st Cir. 1964), *cert. denied*, 380 U.S. 954 (1965).

[13] Ms. Nield's initial impression was fortified when she read the letter: "The impression I had was there was a great sense of urgency in getting the matter resolved. I certainly didn't wish legal action. I would not have wanted a credit rating that would have been detrimental to me." (Tr. 149.)

"Letegram," she thought it was a telegram because of the appearance of the envelope. (Tr. 508 A-509 A). As previously indicated, Ms. Gravatt testified that her impression was that she had received a telegram from Capax. (Tr. 310-311.)[14]

The ALJ found that "Capax' LETEGRAM, as distinguished from its earlier TELEGRAM, is unlikely to deceive ordinary debtors into believing they have received a real telegram. Moreover, it is unlikely to deceive any debtor more than momentarily and certainly not long enough to affect any action." (I.D. 22.) The distinction drawn between "ordinary" and "any" debtors is curious, in light of the fact that the FTC Act protects the public at large, including the most credulous. *Charles of the Ritz* v. *FTC*, 143 F.2d 676, 679-680 (2d Cir. 1944). "The important criterion is the net impression which the [communication] is likely to make upon the general populace." *Id.* Moreover, although the recipients of Capax's dunning material may have "ultimately discerned that the messages were simply debt collection letters in the format of a 'fake' telegram, their initial impression was that they had received a telegram." *Trans World Accounts, supra,* initial decision at 32. The FTC Act is violated if the first contact is secured by deception, even if the consumer becomes aware of the true facts before taking action. *Carter Products, Inc.* v. *FTC*, 186 F.2d 821, 824 (7th Cir. 1951).

Respondents argue that the "Letegram" is an "impact message" which is a legitimate business technique designed to obtain reader interest and attention, and that the communications are in fact urgent because they concern a past due debt which is urgently in need of attention. (Ans. Br. 7-10.) There is no question that the collection of debts is a legitimate business activity. Many creditors understandably consider the collection of past due debts to be urgent. **[10]** However, there may be many reasons for non-payment, including a valid defense to a claimed debt or inability to pay for reasons beyond the debtor's control, and payment may not be exacted by deception or other unfair practices.[15] **[11]**

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[14] We note that respondents' counsel, in describing the consumer witnesses who testified in this proceeding, have stated "all were, by their demeanor and testimony, honest citizens" who comprised "a representative sample of the public at large." (Motion for Directed Verdict, 1 and 17.)

[15] The ALJ's general position was that the format and substance of Capax' letters were mere "bluff and bluster"; in his view, they were disregarded by the recipients, as reflected by the fact that most who testified failed to respond to the letters by making payment. While the legitimacy of the claims which Capax attempted to collect is irrelevant to the legitimacy of its tactics, *cf. Trans World Accounts, supra* at 10 n. 7, the circumstances underlying a number of the claims in the record put perspective on his view. Ms. Thom was dunned for a doctor's bill. The doctor had prescibed tranquilizers for a sore throat. According to Ms. Thom, the tranquilizers had done nothing for the sore throat; the infection spread to her right eye and she lost sight in that eye. (Tr. 117-122.) Mr. Vineburgh was dunned for a bill which he claimed was erroneously sent to him through "bad bookkeeping" and was actually owed by a company for which he was a consultant. (Tr. 416-418, 420.) Ms. Viera had been mistakenly billed by a doctor for an expense owed by her insurance company; she stated that the doctor agreed it was a mistake. (Tr. 491-492.) Ms. Zuccarelli testified that she received dunning letters for a repair bill for what she believed to be a defective central air conditioning unit which had gone through eight condensers in a one year period. (Tr. 635-659.) *See also* Gardner (Tr. 247-248, 288), Gordon (Tr. 353-354, 377-378), Cook (Tr. 506A-507A). Of course, the disputed nature of these bills may not have been representative

(Continued)

Consistent with respondents' argument here, the ALJ stated: "Even though the appearance of a dunning letter may be made similar enough to a telegram to stimulate a conditioned emotional response of urgency and importance, as long as the recipient is aware that he got a gimmick, not a telegram, there is not the deception which turns a Harvard Business School market research problem into a Federal Trade Commission unfair trade practice case." (I.D. 23.) We disagree. There is no evidence that recipients were aware that they had received a gimmick.

In view of the deceptive appearance of its dunning communications, an order provision is necessary to prohibit respondents from using or placing in the hands of others materials which by their appearance misrepresent telegraphic communications. A related order provision is necessary to prevent recurrence in altered form of the violations proven, *Fedders Corp.* v. *FTC*, 529 F.2d 1398 (2d Cir.), *cert. denied*, 429 U.S. 818 (1976). This related provision will prohibit the use or placement in the hands of others of materials which, by simulating telegrams or other methods, forms, or types of communication, misrepresent the nature, import, or urgency of any communication. This remedy is entirely consistent with the Fair Debt Collection Practices Act, Pub. Law 95-109, 15 U.S.C. 1692, which became effective on March 20, 1978. That Act prohibits a debt collector from using "any false, deceptive, or misleading representation or means in connection with the collection of any debt." §807, 15 U.S.C. 1692e.

Under this order, respondents may attempt to attract the recipient's attention in their letters to what their clients believe to be a matter deserving serious consideration, as long as they do not misrepresent the significance or urgency of the message.[16] [12]

II. THE FULL-LINE COLLECTION AGENCY IMAGE

The complaint charged that respondents misrepresented, directly or by implication, that delinquent debtors' accounts had been referred to them as an independent debt collection agency which would engage in typical debt collection activities such as making personal demands for payment and/or filing suit.

Upon review of Capax' communications, we find that Capax clearly

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of the claims pursued by Capax. However, the circumstances underlying them do indicate that these alleged debtors' refusal to pay after receiving Capax' letters may not have been due to dismissal of the letters as mere "bluff and bluster," as the ALJ assumed. Moreover, all of these consumers took some action in response to Capax' letters to protect or defend themselves. *See* n. 33, *infra*.

[16] As to their envelopes, respondents are also circumscribed by the Fair Debt Collection Practices Act, which forbids a debt collector from:

> Using any language or symbol other than the debt collector's address, on any envelope when communicating with a consumer by use of the mails or by telegram, except that a debt collector may use his business name if such name does not indicate that he is in the debt collection business. §808(8), 15 U.S.C. 1692f.

did imply that creditors' claims had been assigned to it for necessary collection action, and that Capax had the authority to take action as the moving party, such as by initiating suit, to collect debts. The following are examples of statements made by Capax in its communications:

> YOUR DELINQUENT ACCOUNT WITH A-B-C- SUPPLY COMPANY HAS BEEN REFERRED TO CONTINENTAL CREDIT CORPORATION FOR ACTION. . . (first contact, Diplomatic series, CX 10(b–c); CX 17(b); Spanish language series, CX 12(b–c); CX 19(b));
>
> . . .CLAIMANT HAS REQUESTED THAT CONTINENTAL CREDIT CORP. RESUME PROCEDURES TO LIQUIDATE THIS CLAIM IN ORDER TO SATISFY THE LIABILITY FOR $9999.99 SET FORTH ABOVE. . . (first contact, Reinstate Diplomatic series, CX 16(b–c));
>
> LEGAL ASSIGNMENT OF YOUR DELINQUENT ACCOUNT HAS BEEN TRANSFERRED TO CAPAX, INC., AND DEMAND IS HEREIN MADE FOR PAYMENT DIRECTLY TO THIS OFFICE IN THE AMOUNT OF $73.50. . . (CX 29(s).)[17] [13]

In assessing the meaning of these communications, we must look to the "impression that is likely to be created," *Kalwajtys* v. *FTC*, 237 F.2d 654, 656 (7th Cir. 1956), *cert. denied*, 352 U.S. 1025 (1957). The impression is to be ascertained not by focusing upon the technical interpretation of each phrase, but by considering the "overall impression" likely to be made on the public. *Murray Space Shoe Corp.* v. *FTC*, 304 F.2d 270, 272 (2d Cir. 1962). We must also keep in mind that deception may be accomplished by innuendo, rather than by outright false statements. *Regina Corp.* v. *FTC*, 322 F.2d 765, 768 (3rd Cir. 1963). The impression likely to be conveyed by Capax' letters is that the company was a collection agency which had been assigned creditors' claims and had the authority to take the action necessary to collect them, such as filing suit. The letters convey the threat that dire consequences will befall the recipient who does not respond, with the innuendo that Capax will be taking the "strong action [which] is often necessary to collect an account."

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[17] Other examples in Capax' letters are:

"A-B-C- SUPPLY COMPANY HAS TURNED OVER TO US THEIR CLAIM AGAINST YOU FOR $999.99. . ." (first contact, Strong series, CX 11(b–d); CX 18(b); Spanish language series, CX 13(b–c); CX 20(b));

"STRONG ACTION IS OFTEN NECESSARY TO COLLECT AN ACCOUNT, ACTION WHICH COULD HAVE BEEN AVOIDED WITH THE DEBTORS COOPERATION. IF YOU CONTINUE TO IGNORE REQUESTS FOR A FRIENDLY DISPOSITION OF THIS CLAIM, YOU MUST ACCEPT THE RESPONSIBILITY FOR FUTURE ACTION";

"THERE IS STILL TIME TO AVOID THE UNNECESSARY CONSEQUENCES OF YOUR NEGLECT. . . (fourth contact, Diplomatic series, CX 10(f); CX 17(e); Spanish series, CX 12(f); CX (e));

". . .IT MAKES NO DIFFERENCE TO US WHETHER YOU PAY VOLUNTARILY OR UNDER COMPULSION. . . . WE HOWEVER TAKE OUR RESPONSIBILITY TO OUR CLIENT SERIOUSLY. . ." (fifth contact, Diplomatic series, and seventh contact, Strong series, respectively, CX 10(g–h); CX 11(k); Spanish series, CX 12(h–i); CX 13(l); CX 18(i); CX 19(g); CX 20(i)).

See also CX 10(e), CX 10(l), CX 11(e), CX 11(k).

That recipients of Capax' letters are likely to gain this false impression was borne out by the consumer testimony: [14]

> Q. [W]ould you tell us whether you recall having had any impressions upon receiving these [communications from Capax]?
>
> A. I was scared to death, as a matter of fact. I got the feeling that someone was either going to come to my door and ask me for the money or I would have to go to court to pay for the check.
>
> Q. Why did you think you would be taken to Court?
>
> A. Well, it said that they had turned [the] account, or whatever over to the Continental Credit. . .
>
> Q. Who did you understand would take you to Court?
>
> A. Continental Credit. (Gravatt, Tr. 311.)

On cross-examination, when asked which particular part of the letter she received led her to believe that such legal action would be taken, Ms. Gravatt replied, "The whole thing." (Tr. 322.) Mr. Gardner, asked who he thought would institute suit against him for a disputed bill, responded:

> A. Capax has indicated throughout this that they were representing [the creditor] and that the claim had been referred to them for action, so I assumed that any action would be instituted, at least, by CAPAX. (Tr. 263.)[18]

Likewise, Ms. Thom testified that she got the impression from Capax' letters that it would be the moving party in taking her to court. (Tr. 118.) The other consumer witnesses all stated that the impression made upon them by Capax' letters was that Capax would be filing suit, taking action to adversely affect their credit ratings, or taking some other harsh action to collect a debt allegedly owed. Ms. Nield (Tr. 171), Ms. Zuccarelli (Tr. 677–679), Mr. Gordon (Tr. 355), Ms. Cook (Tr. 516 A–517 A). [15]

The testimony of Capax' President is noteworthy for its assessment of the impression which would likely be conveyed to the recipients of his company's letters. Mr. Goodman was asked what was meant by the phrase "strong action is often necessary to collect an account," and replied: "Well, I think we are all aware of the credit collection field and that there are all types of actions that are taken. . ." (Tr. 550–551.) He stated that these actions include "harassment, by telephone calls, personal calls, and whatever avenue is open to the creditor." (Tr. 549.)[19]

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[18] Mr. Gardner understood "Legal assignment of your delinquent account has been transferred to CAPAX, Inc., and demand is herein made for payment directly to this office in the amount of $73.50" (CX 29(s)) "to mean that, whereas CAPAX had been acting for Chesapeake [the creditor] up to that point, that now they were acting on their own. In other words, it would be CAPAX who would be suing me rather than Chesapeake." (Tr. 270–271). Mr. Gardner was unaware that Capax did not have the right to sue. (Tr. 271.)

Contrary to the impression conveyed, Capax' service consisted of simply the preparation and mailing of form letters on behalf of creditors to alleged delinquent debtors. As discussed above, there was no assignment of debts to Capax. Capax did not have the authority to file suit in its own name or that of the creditor, and has never brought a suit against any debtor. Capax did not even have the authority to make any telephone calls to debtors or to make other personal contact with debtors demanding payment, and made no such calls or contacts, until the advent of "Phase 2." (Goodman, Tr. 553, 768; Pavlo, Tr. 989–990; Absalom, Tr. 933.)[20] [16]

Thus, Capax misrepresented its true status and authority.[21] There can be little doubt that this misrepresentation was a deceptive practice under the Federal Trade Commission Act. As in a prior debt collection practice case,

> respondents had no authority to collect the debt but only mailed out the forms which were designed to imply that the debt had been turned over to, and was now in the hands of, the transmitting third party for collection. The Commission found that this lack of authority made the letters "wholly grounded in deception," We think this determination was readily supported, . . . for it is quite obvious that the impression conveyed to the debtor is quite different from the actual state of affairs. *S. Dean Slough* v. *FTC*, 396 F.2d 870, 872 (5th Cir. 1968).[22] [17]

The ALJ dismissed this allegation of the complaint on several grounds. First, although he found that Capax represented itself as a collection agency (I.D. 25), he was not convinced that this representation was false (I.D. 26), since its principal activity, dunning debtors, is an important element of the overall collection process (I.D. 28.) It is true that Capax would be considered a collection agency under the Commission's Guides Against Debt Collection Deception, 16 C.F.R. 237,[23] and the Fair Debt Collection Practices Act, § 803(6), 15 U.S.C. 1672a(6).[24] It is also irrefutable that dunning agencies are part of the collection process. However, this misses the point of the allegation; it is not that Capax simply styled itself as a collection agency, but it represented that it had authority to take action which it did not actually possess. Second, the ALJ found that the language of Capax' letters did not operate to deceive debtors. (I.D. 29.) This is clearly belied by the record, as discussed *supra*.

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[19] In a similar vein, which asked what was meant by such phrases in Capax' letters as "unnecessary trouble," "embarrassment," and "additional costs," Mr. Goodman candidly testified that "most people have a very poor impression of collection agencies such as 'debt wagons,' people knocking on doors, speaking to neighbors, and causing all kinds of harassment and this would probably be in [the recipients'] minds." (Tr. 592.)

[20] In its promotional material, Capax stressed that it is "NOT a collection agency" (CX 9(a)); emphasis in original), that the creditor maintains account control and is paid by the debtor directly (CX 9(a)), and that there is no assignment of accounts. (CX 7(a).)

[21] Capax also appears to have misrepresented its internal organization in its letters, for the sake of furthering its image of a full-line collection agency with complete authority to collect debts. At the end of the text of each dunning communication there appeared the name of a person identified as the manager or a person associated with the "collection department," (CX 10(l), CX 11(h–j), CX 12(h–m), CX 13(h–k), CX 16(b–e)), the "credit department" (CX 10(e, f), CX 12(d–g)), or the "claims department" (CX 10(b–d, m), CX 11(b–g, k–n), CX 14(b, c), CX 15(b, c)), yet the testimony reflected that there were no such departments. (Tr. 542, 566.)

[22] *S. Dean Slough* v. *FTC*, *supra*, affirmed the Commission's determination in *State Credit Control Board*, 70 F.T.C. 1318 (1966), prohibiting a collection service from misrepresenting that it had official governmental status, that a delinquent account had been referred to it for collection, or that any legal or other action would be instituted to effect collection. There was broad language in the Commission's opinion which could be construed to mean that any third party referral of a debt which does not confer full authority to collect it is *per se* deceptive. The ALJ here discussed that possible interpretation, noting that it would make the entire dunning business unlawful. (I.D., PP. 50–51.) Such an interpretation would be in error. In *State Credit Control Board*, as here, the Commission prohibited the representation that the third party collection service has the authority to take legal or other affirmative collection action, when such is not the case. The Commission's final order established as a defense that respondent has the authority and good faith intent to take any represented action.

Finally, respondents argue that the letters sent to debtors are merely "reminders" of their outstanding bills. (Ans. Br. 23.) There is nothing wrong with mere reminders, but they must accurately portray the situation and not convey a misleading impression, directly or by implication.

To ensure that law violations of the sort found here do not continue, our order will prohibit respondents from misrepresenting their status, activities, or actions. If respondents can establish that such representations are factually correct, that shall serve as a defense. [18]

III. THREATS OF SUIT

According to the complaint, respondents represented that unless payment was received, steps would be taken to initiate legal action against the debtor, but that in fact the only action taken during the form letter series was to send additional letters to the debtor or to return the uncollected account to the creditor. The ALJ found, and letters introduced in the record clearly demonstrate, that threats of legal action were made. For example,

> . . .IT IS THE INTENTION OF OUR CLIENT TO EXHAUST EVERY LEGAL AVENUE AT THEIR DISPOSAL IN ORDER TO COLLECT THIS CLAIM. (sixth, second, eighth and second contacts, respectively, Diplomatic and Strong series, (CX 10(i); CX 11(d); CX 17(h); CX 18(c); Spanish series, CX 12(j); CX 13(d));

> . . .IMPERATIVE THAT SATISFACTORY ARRANGEMENTS BE MADE TO AVOID FURTHER ACTION, AVAILABLE TO CLAIMANT UNDER PROVISIONS OF STATE STATUTES. . . (seventh contact, Diplomatic series, sixth contact, Strong series, respectively, CX 10(j)-(k); CX 11(i)-(j); CX 18(h); Spanish series, CX 12(k)-(l); CX 13(k); CX 19(i); CX 20(h));

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[23] Section 237.0(f) defines a "collection agency" as "any. . . corporation. . .which collects money debts for others." Section 237.0(a) defines "industry member" as "any. . .corporation. . . engaged in the practice of collecting or attempting to collect any and all kinds of money debts for itself or others. . . ."

[24] "The term 'debt collector' means any person who uses any instrumentality of interstate commerce or the mails in any business the principal purpose of which is the collection of any debts, or who regularly collects or attempts to collect, directly or indirectly, debts owed or due or asserted to be owed or due another."

YOUR REFUSAL OR NEGLECT TO SATISFY THE ABOVE LIABILITY COMPELS US TO NOTIFY YOU TO PRESENT ANY DEFENSE AGAINST THE VALIDITY OF THIS CLAIM ON FILE. YOU MAY PROTEST SAID CLAIM OR LIST PROPERTY WHICH YOU FEEL MAY BE EXEMPT, IF A-B-C- SUPPLY COMPANY OBTAINS A JUDGMENT. (ninth contact, Diplomatic and Strong series, tenth contact, Diplomatic and Strong series, respectively, CX 10(m); CX 11(n); CX 17(k); CX 18(k); Spanish series, CX 12(n); CX 13(m)-(n); CX 19(k); CX 20(j));

WE ARE WRITING THIS LETTER TO INFORM YOU OF THE SERIOUSNESS OF YOUR DELINQUENCY AND OF THE FACT THAT SHOULD IT CONTINUE ALL POSSIBLE LEGAL MEANS WILL BE TAKEN TO COLLECT IT. (third contact, Strong series, CX 11(e); CX 18(d); Spanish series, CX 13(e); CX 20(d).[25]

The ALJ concluded, however, that these statements were not deceptive. First, he found that "most" of the statements plainly refer to a suit by the creditor rather than by Capax. (I.D. 45.) However, there are some statements, such as the last, which do not state who will be suing, and carry the innuendo that "we," Capax, will be using all possible legal means to collect the alleged debt. Such statements are patently deceptive, in view of Capax' lack of authority to initiate legal action against a debtor. Those statements threatening legal action by the creditor also have the capacity to deceive, since Capax had no knowledge during the course of its flat [20] rate series whether a creditor actually would take legal action against the particular debtor. (Tr. 543, 567, 587-590, 600-601.) It is a deceptive trade practice for a collection service to threaten the initiation of legal proceedings against a debtor, either by itself or another, where there is in fact no intent to actually initiate such proceedings. *Cf. Trans World Accounts, supra; Wilson Chemical Co.*, 64 F.T.C. 168, 185 (1964); *see also* § 807(5) of the Fair Debt Collection Practices Act, which prohibits the threat to take any action that cannot legally be taken or that is not intended to be taken. 15 U.S.C. 1692e.

The impression of the witnesses who received Capax' communications was that legal action would definitely be commenced unless their alleged debts were paid. (Thom, Tr. 128-130, 142; Nield, Tr. 151, 154; Gardner, Tr. 263; Gravatt, Tr. 321-322; Vineburgh, Tr. 437.) For example, when Ms. Thom was asked what statement in CX 18(c) led her to believe that she would be sued, she replied: "It is the intention of our client to exhaust every legal means at their disposal." (Tr. 128.) She elaborated: "I got the impression that it was Continental Credit

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[25] Additional examples are:

". . .IF YOU WANT TO AVOID UNPLEASANT AND COSTLY ACTION, MAKE IMMEDIATE PAYMENT DIRECTLY TO A-B-C- SUPPLY COMPANY (eighth contact, Diplomatic series, sixth contact, Strong series, respectively, CX 10(l); CX 18(g); Spanish series, CX 13(i); CX 19(j); CX 20(g));

"IT IS IMPERATIVE THAT YOU CONTACT YOUR CREDITOR TODAY TO AVOID FURTHER ACTIONS. . ." (fifth, sixth and second contacts, respectively, Diplomatic and Strong series, CX 10(g)-(h); CX 17(g); CX 18(c); Spanish series, CX 12(h)-(i); CX 13(d).)

See also CX 10(i), CX 11(h), CX 11(k).

Corporation. . .that was going to sue us." (Tr. 128.) "We called Continental Credit Corporation because we sincerely felt they were going to sue us, they were going to take us to court. . ." (Tr. 129.)[26] [21]

The ALJ further ruled that while Capax did not know whether particular creditors intended to bring suit against particular debtors, Capax "did have a *reasonable basis* for warning debtors to expect suit if they did not pay up, in its knowledge that creditors generally and Capax' clients in particular, almost without exception, want to sue for their money if necessary, assuming a negligible economic feasibility factor." (I.D. 49.) The ALJ relied heavily on the testimony of Mr. Goodman, Capax' President, for the finding. He acknowledged that Mr. Goodman admitted that when a dunning letter is transmitted with a warning that suit would be brought Capax could not really say "for a fact" whether the particular creditor would sue if the debt went unpaid (Tr. 543, 588, 590); the ALJ concluded, however, that Mr. Goodman's testimony indicated there was a reasonable basis for such warnings. We disagree. After stating generally that he believed his clients intended to exhaust all possible legal means to recover a claimed debt, upon cross-examination he conceded that "we *assume* they want the money in" (Tr. 567, emphasis added), "This is *normally implied* to us by the creditor" (Tr. 588, emphasis added), and "We are under the *impression* given to us by our clients that they would [bring suit] when financially feasible to do so." (Tr. 589, emphasis added). Assumptions, implications, and impressions hardly furnish a reasonable basis. Moreover, nothing in the record provides any grounds for the finding made by the ALJ that creditors generally, and Capax' clients in particular "almost without exception," desire to sue to recover claimed debts "assuming a negligible economic feasibility factor." Assuming that such a feasibility factor exists, the record provides no indication as to whether it is "negligible" and, if so, what that amounts to.

We hold that respondents, as charged in the complaint, falsely threatened that legal action would be initiated unless payment was received. The position of the ALJ and respondents—that the threat of legal action is a "largely reasonable and justifiable prediction" (Ans. Br. 23)—must be rejected, for the net impression of Capax' representations was that legal action definitely would be commenced, and respondents [22] admit they did not know this.[27] As the court stated in *S. Dean Slough* v. *FTC*, *supra* at 872, "the fault with Petitioner's position is his own readily-made admission that the entire collection scheme is designed to collect without the necessity of legal action, and therein lies the deception."

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[26] The ALJ dismissed much of this consumer testimony because he interpreted many of the particular phrases to which the witnesses had referred as warning only of a possibility of suit, and concluded that such a warning was literally true. However, as discussed above, in ascertaining the impression created by communications, the overall impression likely to be made upon the public, not the technical interpretation of each phrase, is crucial. *Murray Space Shoe Corp.* v. *FTC*, 304 F.2d 270, 272 (2d Cir. 1962). The meaning conveyed by words often differs from their literal significance; a debt collector may not exploit this disparity to deceive by using words which may be literally true but convey a false message to the reader. *Cf. J. B. Williams Co.* v. *FTC*, 381 F.2d 884, 889 (6th Cir. 1967). A fair reading of the testimony here reflects that these witnesses, in fact, were testifying as to their overall impressions from Capax' letters that suit would definitely be brought against them.

These allegations of the complaint having been sustained, the Commission's order will prohibit respondents from misrepresenting directly or by implication that legal action with respect to an alleged delinquent debt may or will be initiated, or otherwise misrepresenting in any manner the likelihood of legal action. The factual truth of such representation will provide a defense to respondents, but references to legal action in their letter series must be carefully and selectively employed to avoid deception. *See Trans World Accounts, supra* at 12–13. Respondents should not represent, directly or by implication, that legal action *will* be taken or *is intended* to be taken unless such action is taken in all cases where the threat of legal action is not met by payment. *Helix Marketing Corporation*, 83 F.T.C. 514 (1973). Furthermore, respondents should not represent, directly or by implication, that legal action *may* be taken unless they can demonstrate from their experience that suit is the *ordinary* response to nonpayment. *Cf.* Fair Debt Collection Practices Act, § 805(c)(2), 15 U.S.C. 1692c. Suit in more than half the instances of nonpayment will be sufficient to substantiate a claim that legal action may be taken. *Trans World Accounts, supra; Helix Marketing Corp., supra.* In order to facilitate compliance with the order, respondents might well treat discernible classes of alleged debtors differently, depending upon the likelihood that members of each class will be sued. "Unsatisfied claims of a particular client or clients should not be lumped together for the purpose of establishing that legal action is taken in more than 50 percent of all cases where it is the practice to treat different classes of claims in different ways." *Trans World Accounts, supra.* If claims below a certain amount are not ordinarily pursued by some creditors in court, the letters used to collect those claims should not contain references to legal action, except where a decision to sue has been made. [23]

IV. THREATS TO CREDIT STANDING

Capax' dunning letters contained the following statements:

> PAID IN FULL WITHIN SEVEN DAYS, THIS ACCOUNT WILL NOT BE SHOWN ON OUR CREDIT RECORDS. . . . FORWARD YOUR PAYMENT NOW DIRECTLY TO A–B–C– SUPPLY COMPANY IN ORDER TO RECEIVE PROPER CREDIT. . .

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[27] Capax admits that it never even provided any advice with respect to possible legal action until the flat rate letter service had run its course. (Tr. 766–767; 596–601.)

(first contact, Diplomatic series, CX 10(b)–(c); CX 17(b); Spanish series, CX 12(b)–(c); CX 19(b));

UP TO NOW YOUR CREDIT STANDING WITH A–B–C– SUPPLY COMPANY HAS BEEN SATISFACTORY. CREDIT IS A PRIVILEGE, NOT A RIGHT. IT IS IMPORTANT TO PROTECT THIS PRIVILEGE, BECAUSE ONCE IT IS LOST IT IS ALMOST IMPOSSIBLE TO REPLACE. LIKE MOST OTHER PRIVILEGES, YOU ONLY MISS IT WHEN YOU NEED IT. (third contact, Diplomatic series, fifth contact, Diplomatic series, second contact, Bad check series, respectively, CX 10(e); CX 17(f); CX 21(c); Spanish series, CX 12(g); CX 19(f));

IF THIS IS NOT DONE [*i.e.*, making a satisfactory arrangement for payment] CONTINENTAL CREDIT CORPORATION CAN TAKE NO OTHER POSITION BUT TO RECOMMEND A STRONGER COURSE OF ACTION TO OUR CLIENT. . . IF THIS IS DONE THERE MAY BE ADDITIONAL COSTS TO YOU AND YOUR CREDIT STANDING MAY SUFFER. . . . (fourth contact, strong series, CX 11(f–g); CX 18(e); Spanish series, CX 13(g); CX 20(e).)[28] [24]

In our judgment, these statements have the capacity to deceive recipients into believing that unless payment is received, respondents will take action to adversely affect the debtor's credit record, as alleged in the complaint. Respondents had no control over or knowledge of whether a creditor would take action to adversely affect the debtor's credit standing if payment was not received, and Capax never took any such action itself.

The ALJ dismissed this allegation of the complaint because he considered the literal meaning of the above-quoted statements to be true: in the first instance, if payment is made, the account will not be shown on Capax' credit record; in the second instance, if payment is not made, the debtor's credit standing with the particular creditor involved will suffer; and in the third instance, nonpayment will have an adverse effect on the debtor's credit standing if a law suit is brought. These are possible meanings, but the statements can also easily be interpreted to mean that failure to make payment will adversely effect the debtor's general credit standing. Representations capable of two meanings, one of which is false, are misleading. *United States* v. *95 Barrels of Vinegar*, 265 U.S. 438, 442 (1924); *Rhodes Pharmacal Co.* v. *FTC*, 208 F.2d 382, 387 (7th Cir. 1953), *modified on other grounds*, 348 U.S. 970 (1955). Such representations are to be construed against those making them. *United States* v. *95 Barrels of Vinegar, supra; Murray Space Shoe Corp.* v. *FTC*, 304 F.2d 270, 272 (2d Cir. 1962).[29] The testimony of the witnesses amply supports our view. [25]

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[28] Capax' "Telegram" made the following statement:

"IN AN EMERGENCY, WHEN YOU NEED CREDIT WILL YOU BE ABLE TO GET IT OR BE TURNED DOWN BECAUSE OF YOUR PAST EXPERIENCE. . . . THIS IS SOMETHING TO THINK ABOUT. . . . IT IS YOUR CREDIT FUTURE THAT MAY SUFFER. . . ." (CX 17(d).)

[29] The ALJ considered it to be significant that Capax' letters made no "reference to consumer reporting agencies

(Continued)

Capax' President, Mr. Goodman, admitted that the phrase "your credit standing may suffer" could be interpreted to mean that the debtor's general credit standing could be adversely affected. (Tr. 593–596.) This was vividly illustrated by the testimony of the consumers who received Capax' letters. Mr. Gardner interpreted the statements regarding credit records to mean that failure to pay the alleged debt "would affect my credit in a derogatory manner." (Tr. 252; *see generally* Tr. 250–253, 289–294.)[30] Mr. Gordon was concerned from Capax' letters that "some action would be taken against my credit rating." (Tr. 355; *see also* Tr. 375–376, 381–385, 398.)[31] Mr. Vineburgh had the impression from Capax' letters that if he did not pay the bill "they were going to initiate action that would reflect on my credit and I had just gone through a rather traumatic experience a few years previously (from a substantial loss caused by riots in Washington, D.C.) and I didn't want any other reflections on my credit." (Tr. 420–421.) Ms. Viera "had the feeling that my credit was going to be harmed. . . ." (Tr. 493; *see generally* 493–499.)

It is a deceptive practice to falsely represent that a debtor's credit rating will be adversely affected if the debt is not paid. *Cf. Parents' Magazine Enterprises, Inc.*, 68 F.T.C. 980 (1973). Our order will prohibit respondents from representing that action will be taken to adversely affect the debtor's credit record with a consumer reporting agency or any other third party, or otherwise misrepresenting the impact or effect of nonpayment upon the debtor's credit record. **[26]**

V. THREATS TO ENFORCE PROMPT PAYMENT

The ALJ dismissed the final allegation of the complaint, charging respondents with misrepresenting that unless payment was received within the time specified, immediate action would be taken to collect the debt, such as the filing of suit. The complaint asserted that the only subsequent action was either the sending of additional form letters to the alleged debtor or returning the uncollected account to the creditor. We believe that the evidence amply supports the complaint allegation.

Capax' letters were replete with threats, both explicit and implicit,

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or the credit ratings they dispense." (I.D. 51; *see generally* I.D. 54–54.) However, the precise manner in which one's credit standing would be adversely affected—whether due to the action of a consumer reporting agency or otherwise—would probably be irrelevant to most consumers, since it is fair to assume that the general public is not terribly familiar with the manner in which credit ratings are made and the role played by consumer reporting agencies. The FTC Act "was not made for the protection of experts, but for the public." *Charles of the Ritz* v. *FTC*, *supra* at 679. For those consumers who would relate an adverse effect upon one's credit record to the activities of a consumer reporting agency, the inference could certainly be drawn from Capax' statements that nonpayment would result in respondents' taking action to adversely affect the debtor's credit record with a consumer reporting agency.

[30] Mr. Gardner assumed that Capax was possibly "in a position to affect my credit generally." (Tr. 294.) We find that Capax' statements have the capacity to create that assumption.

[31] Mr. Gordon did not know, of course, that Capax did not take any action to adversely affect a debtor's credit rating. (Tr. 404–405.)

that imminent adverse action awaited the debtor who failed to meet a deadline.

. . .YOUR CREDITOR HAS REQUESTED THAT YOU BE GIVEN SEVEN DAYS TO SETTLE THIS ACCOUNT. . . (first contact, Diplomatic series, CX 10(b–c); CX 17(b); Spanish series, CX 12(b–c); CX 19(b));

. . .URGENT. . .IMMEDIATELY CONTACT A–B–C– SUPPLY COMPANY. . .IF SETTLEMENT IS NOT MADE WITHIN 48 HOURS UPON RECEIPT OF THIS LETEGRAM, WE SUGGEST YOU CONTACT YOUR ATTORNEY TO DETERMINE YOUR LEGAL LIABILITY. . . ." (seventh contact, Diplomatic series, seventh contact, Strong series, eighth contact, Diplomatic series, seventh contact, Strong series, CX 10(j–k); CX 11(i–j); CX 17(i); CX 18(h); Spanish series, CX 12(k–l); CX 13(j–k); CX 19(i); CX 20(h));

WE CAN WAIT NO MORE THAN 5 DAYS TO HEAR FROM A–B–C– SUPPLY COMPANY ON SETTLEMENT. YOUR IMMEDIATE RESPONSE IS IMPERATIVE. (eighth contact, Diplomatic series, ninth contact, Diplomatic series, sixth contact, Strong series, respectively, CX 10(l); CX 17(j); CX 19(g); Spanish series, CX 12(m); CX 13(i); CX 19(j); CX 20(g)); [27]

YOU MAY IMMEDIATELY REGISTER YOUR DEFENSE, IN WRITING, WITHIN 48 HOURS AFTER RECEIPT OF THIS NOTICE, WITH YOUR CREDITOR. . . (ninth contact, Diplomatic series, ninth contact, Strong series, tenth contact, Strong series, respectively, CX 10(m); CX 11(n); CX 18(k); Spanish series, CX 12(n); CX 13(m–n); CX 19(k)).[32]

The ALJ dismissed most of the representations as irrelevant to the complaint allegation because they did not specify what would happen if the debtor did not pay. This omission appears to us to be by design, and the ambiguity may make the ultimatum more ominous. "Representations can be contrived to mislead not only by what they contain but [28] by what they omit." *Manco Watch Strap Co.*, 60 F.T.C. 495, 510 (1962). The ALJ recognized that a number of the statements warned the debtor that some sanction, such as suit, will be invoked if a specific new deadline is not met.

Contrary to Capax' representations, a debtor's failure to meet a deadline would usually result in no more than receipt of the next letter in the series. As we have noted, Capax had no authority to take action, immediate or otherwise, to force payment. Likewise, it had no knowledge of or control over any action which might be taken by the creditor to recover an alleged debt. Mr. Goodman, Capax' President, admitted that the only consequence of the debtor's failure to pay before the indicated deadline would be the transmittal of further letters. (Tr. 562, 579.) For example, if the recipient failed to "settle" the account within the seven days specified by letter CX 10(b), "in all probability he would receive another contact." (Tr. 534.) Capax generally never suggested to its clients to stop the mailing of letters until the series had been completed. (Tr. 799–802.) The purpose of the specific deadlines for payment was to establish a "time frame" (Tr. 535) to get the debtor "off his rump" (Tr. 604–605) so that he would pay as soon as possible (Tr. 535). At the oral argument, respondents' counsel conceded that the deadlines imposed by Capax were arbitrary. (TROA 54.)

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[32] Other examples are:

". . .IF NOT PAID WITHIN ONE WEEK, TO LIQUIDATE THIS MATTER WE WILL BE FORCED TO RECOMMEND ACTION WHICH MAY MEAN ADDED COSTS TO YOU. . . .PROMPT ACTION IN THIS MATTER IS IMPERATIVE. MAKE IMMEDIATE PAYMENT DIRECTLY TO A–B–C– SUPPLY COMPANY. . ." (first contact, Strong series, CX 11(b–c); CX 18(b); Spanish series, CX 13(b–c); CX 20(b);

". . .THE SEVEN DAY COURTESY PERIOD HAS EXPIRED. . . .IT IS IMPERATIVE THAT YOU CONTACT YOUR CREDITOR TODAY TO AVOID FURTHER ACTION. . ." (second contact, Strong series, CX 11(d); CX 18(c); Spanish series, CX 13(d); CX 20(c));

"LITTLE TIME REMAINS. . ." (third contact, Diplomatic series, fifth contact, Diplomatic series, second contact, Bad check series, respectively, CX 10(e); CX 17(f)).

See also CX 10(g–h), CX 11(f–g), CX 11(k), CX 11(l–m), CX 11(n), CX 14(b–c).

The ALJ found that Capax' warnings of immediate sanctions if its payment deadlines were not met may be false in "a literal sense," but that the ordinary debtor would recognize them as mere "bluff and bluster," analogous to puffing in merchandising, which can be taken with a "grain of salt." (I.D. 64–68.) He believed that the "debtor here—like debtors generally—learn that such threats are commonly harmless and may commonly be disregarded for a long time, at least—with impunity." (I.D. 64.) Such an approach is unprecedented in Commission annals, and for good reason. There is absolutely no support in the record for the assumptions made by the ALJ. On the contrary, the record reflects that debtors receiving dunning letters demanding payment within a deadline experience great anxiety and apprehension. The testimony of the recipients here indicates that their refusal to pay their debts was frequently due to serious disputes with the creditors or [29] erroneous billing, *see* n. 15 *supra*, rather than disregard of the threats by Capax as harmless. In fact, the general reaction of the dunned consumers was to take some action to protect or defend against the threat of imminent action by Capax.[33] Of course, it is well

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[33] Upon receiving Capax' dunning letters specifying deadlines for payments, Ms. Thom took steps to defend herself against anticipated legal action, contacting an attorney. (Tr. 120–122.) She testified that the message contained in letter CX 18(d), which states that "all possible legal means will be taken to collect" the debt and directs that payment be made within the next few days, "strikes terror into your heart." (Tr. 130.) Ms. Zuccarrelli was "shocked" (Tr. 671) and "worried" (Tr. 662) by Capax' letters demanding payment for an air conditioning repair bill which she disputed. She testified that "each and every time I went to Florida [where the house with the air conditioner was located] I called the tax assessor's office to find out if a lien had been put against my property down there and also in New Jersey" (where her permanent residence was located). (Tr. 664.) From Capax' letters, Mr. Gordon feared that some action would be taken against his credit rating and called his attorney, who made the determination to contact Capax' regarding the matter. (Tr. 354–361.) Ms. Nield had the overall impression from Capax' communications that a legal suit would be commenced against her immediately, and contacted the creditor. (Tr. 151–152.) Mr. Gordon "thought some detrimental action was going to be taken, so I forwarded each letter and letegram to my attorney for his recommendation on the answers he saw fit." (Tr. 373–374.) Ms. Viera believed that the dunning letters she received were a mistake because her insurance company owed the medical bill for which she was being dunned, but was afraid that her credit standing would be harmed by Capax and anxiously contacted the doctor. (Tr. 491–496.) Mr. Gardner

(Continued)

established that capacity to deceive rather than actual deception is the standard under Section 5, and that whether or not consumers are misled into making payment or suffering injury is irrelevant if the practices under consideration have the capacity to deceive. *See, e.g., Thiret* v. *FTC,* 512 F.2d 176, 180 (10th Cir. 1975); *Mohawk Refining Corp.* v. *FTC,* 263 F.2d 818, 821 (3rd Cir.), *cert. denied,* 361 U.S. 814 (1959); *Goodman* v. *FTC, supra.* [30]

Our order will prohibit Capax from misrepresenting the imminency of any action that may be taken.

VI. AFFIRMATIVE DISCLOSURE

Complaint counsel request that the order require the following type of notice in each communication sent to alleged debtors:

> We are an independent company employed by your creditor solely for the purpose of reminding you of your outstanding obligation. We are not authorized to engage in typical debt collection activity, to institute suit or to take any action which may affect your credit rating. (App. Br. 54–55, n. 61.)[34]

Capax concedes that if its "Telegram" and "Letegram" formats are found deceptive they should be banned, as should the misrepresentations regarding the full-line collection agency image, threats of suit, threats to credit standing, and threats to enforce prompt payment. (Ans. Br. 31–32.) It argues, however, that the notice might suggest to debtors that nothing of importance can be expected from Capax' communications, to their obvious peril if suit is brought by the creditor. [31]

While the Commission's authority to require affirmative disclosure is well established, *see, e.g., Ward Laboratories, Inc.* v. *FTC,* 276 F.2d 952 (2d Cir.), *cert. denied,* 364 U.S. 827 (1960), we do not consider the affirmative disclosure sought here by complaint counsel to be necessary, under the circumstances of this case, in light of the order's ample prohibitions on misrepresentations. Moreover, we believe that the proposed disclaimer could lull recipients into a false sense of security by giving them the impression that failure to pay the claimed debt will not result in legal action or harm to their credit standing. Because creditors might pursue an alleged delinquent debt by bringing

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interpreted Capax' letters to threaten suit in the immediate future, and contacted his lawyer as well as a state consumer protection office. (Tr. 263–264.) The reactions of the dunned consumers who testified hardly supports the view that they considered Capax' threats to enforce prompt payment as mere bluff and bluster to be disregarded.

[34] This is a modification from the proposed affirmative disclosure in the notice order accompanying the complaint. The proposed affirmative disclosure would not be required where respondents indicate in a particular communication that (1) suit will be filed and it is, unless failure to file suit is due to subsequent bona fide instructions from the creditor or subsequent information from the debtor indicating non-existence of the alleged debt, or (2) some bona fide action against the debtor will be taken (other than filing suit or mailing subsequent requests for payment) and that action is, in fact, taken. (Notice Order, ¶ 4; App. Br. 54–55.)

suit or could report the matter to a consumer reporting agency, debtors who decided not to make payment on the basis of the disclaimer could suffer harm. Therefore, our order will not include the proposed affirmative disclosure.[35]

For the foregoing reasons, the appeal of complaint counsel is granted, as provided above. The initial decision of the administrative law judge dismissing the complaint will be vacated, and an appropriate order will be entered.

FINAL ORDER

This matter having been heard by the Commission upon the appeal of complaint counsel from the initial decision, and upon briefs and oral argument in support thereof and in opposition thereto, and the Commission, for the reasons stated in the accompanying opinion, having granted the appeal:

It is ordered, That the initial decision and order of the administrative law judge be, and they hereby are, vacated, except to the extent that the initial decision is consistent with the accompanying opinion of the Commission, and the findings of fact and conclusions of law contained in the opinion be, and they hereby are, adopted as the findings and conclusions of the Commission in this matter.

Accordingly, the following cease and desist order is hereby entered:

ORDER

It is ordered, That respondents Capax, Inc., formerly Continental Credit Corporation, Inc., a corporation, its successors and assigns, and its officers, and Joseph V. DeFelice and Arnold Goodman, individually and as officers of said corporation, and Norman Bricker, individually and as a former officer of said corporation, and respondents' agents, representatives, and employees, directly or through any corporation, subsidiary, division, or other device, in connection with the offering for sale, sale, or distribution of any service or printed matter for use in the collection, or attempting to collect, or assisting in the collection of, or inducing or attempting to induce the payment of alleged delinquent debts in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

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[35] As complaint counsel note (App. Br. 59, n. 62), the Commission has previously ordered disclaimers similar to that sought here. *Trans-American Collections, Inc.*, Dkt. 8901, 83 F.T.C. 525 (1973); *United Compucred Collections, Inc.*, Dkt. C-2806, 87 F.T.C. 542 (1976); *Trans National Credit Corp.*, Dkt. C-2807, 87 F.T.C. 549 (1976); *Continental Collection Bureau of America, Inc.*, Dkt. C-2808, 87 F.T.C. 557 (1976); *North American Collections, Inc.*, Dkt. C-2809, 87 F.T.C. 566 (1976); *Power's Service, Inc.*, Dkt. C-2810, 87 F.T.C. 574 (1976); *Continental Collection Service*, Dkt. C-2811, 87 F.T.C. 582 (1976). The appropriateness of those disclaimers depends upon the facts of each case, including the prescribed language and the details of the firm's operations and authority. However, we are today issuing orders to show cause why those consent orders should not be modified to delete the mandated affirmative disclosures, pursuant to Commission Rule 3.72(b).

1. Using or placing in the hands of others for use, envelopes, letters, forms, or any other materials which by their appearance, content, or otherwise, misrepresent that they are telegraphic communications.

2. Using or placing in the hands of others for use, envelopes, letters, forms, or any other materials which by simulating telegrams or other methods, forms, or types of communication misrepresent the nature, import, or urgency of any communication.

3. Representing, directly or by implication, that:

(a) Delinquent debtors' accounts have been referred to respondents or another as a debt collection agency with authority to engage in such debt collection activities as making personal demands for payment and/or filing suit; or otherwise misrepresenting respondents' status, activities, or actions.

(b) Unless payment is received, legal action with respect to an alleged delinquent debt may or will be initiated, or otherwise misrepresenting in any manner the likelihood of legal action..

(c) Unless payment is received, action will be taken to adversely affect the debtor's credit record with a consumer reporting agency or any other third party; or otherwise misrepresenting the impact or effect of nonpayment upon the debtor's credit record.

(d) Unless payment is received within the time specified by respondents, immediate action will be taken to collect the debt, such as the filing of suit; or otherwise misrepresenting the imminency of any action that may or will be taken.

Provided, that it shall be a defense in any enforcement proceeding initiated under Paragraph 3 for respondents to establish that such representations are factually correct.

4. Placing in the hands of others the means and instrumentalities to accomplish any of the matters prohibited in this order, or which fail to comply with the requirements of this order.

It is further ordered, That the respondent corporation shall distribute a copy of this order to each of its operating divisions or departments and to each of its present and future officers, agents, representatives, or employees engaged in any aspect of the offering for sale, sale, or distribution of any service or printed matter for use in the collection, or attempting to collect, or assisting in the collection of, or inducing or attempting to induce the payment of alleged delinquent debts, and that said respondent secure a signed statement acknowledging receipt of said order from each such person.

It is further ordered, That the respondent corporation notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent such as dissolution, assignment, or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any other change in the corporation which may affect compliance obligations arising out of the order.

It is further ordered, That the individual respondents named herein promptly notify the Commission of the discontinuance of their present business or employment and of their affiliation with a new business or employment. In addition, for a period of ten years from the effective date of this order, the individual respondents named herein shall promptly notify the Commission of their affiliation with a new business or employment whose principal activities include the offering for sale, sale, or distribution of any service or printed matter for use in the collection of, or attempted collection of, or for assisting in the collection of, or for inducing or attempting to induce the payment of alleged delinquent debts, or of their affiliation with a new business or employment in which their duties and responsibilities involve the offering for sale, sale, or distribution of any service or printed matter for use in the collection of, or attempted collection of, or for assisting in the collection of, or for inducing or attempting to induce the payment of alleged delinquent debts. Such notice shall include individual respondents' current business address and a statement as to the nature of the business or employment in which they are engaged as well as a description of their duties and responsibilities. The expiration of the notice provision of this paragraph shall not affect any other obligation arising under this order.

It is further ordered, That the respondents herein shall, within sixty (60) days from the date this order becomes final, and periodically thereafter as required by the Federal Trade Commission, file with the Commission a written report setting forth in detail the manner and form of their compliance with this order.

IN THE MATTER OF

NOSOMA SYSTEMS, INC., ET AL.

MODIFYING ORDER IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2841. Final Order, Sept. 28, 1976 — Modifying Order, June 12, 1978

This order modifies an order to cease and desist issued on September 28, 1976, 41 FR 50810, 88 F.T.C. 459, by adding particular language to the fourth paragraph of the original order to prevent conflict with the Fair Debt Collection Practices Act.

ORDER GRANTING PETITION TO REOPEN PROCEEDING AND MODIFY ORDER TO CEASE AND DESIST

By letter filed on March 27, 1978, petitioners have requested the Commission to modify the consent order to cease and desist. This request is being treated as a petition to reopen the proceeding and modify the order under Rule 3.72(b)(2) of the Commission's Rule of Practice.

Petitioners seek to modify Paragraph Four of the order so that it is not in conflict with the Fair Debt Collection Practices Act. The Bureau of Consumer Protection does not oppose the modification. Therefore,

It is ordered, That the proceeding be reopened for the purpose requested.

It is further ordered, That Paragraph Four be modified by the addition of the following language:

> *Provided, however*, that nothing in this paragraph, shall be interpreted as violating the order when in acquiring location information, as that term is defined in Section 803(f) of the Fair Debt Collection Practices Act, the caller identifies his employer, when expressly requested to do so pursuant to Section 804(1) of said Act.

IN THE MATTER OF

HIKEN FURNITURE COMPANY

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION AND TRUTH IN LENDING ACTS

Docket C-2923. Complaint, June 12, 1978 — Decision, June 12, 1978

This consent order, among other things, requires a Belleville, Ill. furniture retailer to cease employing bait and switch tactics, and misrepresenting or failing to make relevant disclosures regarding prices, products and service, cooling-off periods, cancellation and refund rights, and the availability of arbitration to resolve consumer disputes. The order further prohibits the use of unfair or deceptive means to induce payment from allegedly delinquent debtors, and requires respondent to provide, in the extension of credit, those materials and disclosures required by Federal Reserve regulations. Additionally, respondent is required to furnish its advertising media with copies of Commission's press release setting forth the terms of the order.

Appearances

For the Commission: *Richard A. Palewicz.*

For the respondent: *Neil N. Bernstein, St. Louis, Mo.*

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and of the Truth in Lending Act and the implementing regulation promulgated thereunder, and by virtue of the authority vested in it by said Acts, the Federal Trade Commission, having reason to believe that Hiken Furniture Company, a corporation, hereinafter sometimes referred to as respondent, has violated the provisions of said Acts, and the implementing regulation promulgated under the Truth in Lending Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent Hiken Furniture Company is a corporation organized, existing and doing business under and by virtue of the laws of the State of Illinois, with its principal office and place of business located at 218 West Main St., Belleville, Illinois.

PAR. 2. Respondent is now, and for some time last past has been engaged in the advertising, offering for sale, sale and distribution of household furniture and appliances, and services in connection therewith to the general public.

COUNT I

Alleging violations of Section 5 of the Federal Trade Commission Act, the allegation in Paragraphs One and Two hereof are incorporated by reference in Count I as if fully set forth verbatim.

PAR. 3. In the course and conduct of its aforesaid business, respondent has disseminated and caused the dissemination of certain advertisements concerning said products and services by various means in or affecting commerce as "commerce" is defined in the Federal Trade Commission Act, including, but not limited to, advertisements inserted in newspapers of interstate circulation, and in radio and television broadcasts of interstate circulation, for the purpose of inducing, and which was likely to induce, directly or indirectly, the purchase of said products and services; additionally, respondent owns, operates and controls a total of two (2) retail furniture stores located in the States of Illinois and Missouri.

PAR. 4. In the course and conduct of respondent's business and for the purpose of inducing the sale of its household furniture, appliances and services in connection therewith, respondent has made numerous statements and representations in newspaper advertisements, radio and television commercials and oral statements by salesmen to prospective customers.

Typical and illustrative of said statements and representations, but not all inclusive thereof, are the following:

> HIKEN WAREHOUSE SALE
>
> 3 DAY RIOT SALE
>
> HIKEN 2 DAY SALE
>
> *IF YOU WANT TO SAVE $100 $200 $300 $400* BUY NOW . . .
>
> SAVE UP TO 50% AND MORE
>
> EXTRA EXTRA SAVINGS
> SAVE 20% to 60% & MORE
>
> 2-PIECE SPANISH STYLE
> LIVING ROOM Reg. $399.00
> $199
>
> HUGE SELECTION
>
> WE BOUGHT CARLOADS OF MERCHANDISE. . .
>
> IMMEDIATE
> AVAILABILITY
> NO WAITING

. . .GIANT FURNITURE VALUES. . .

GIGANTIC VALUE!

NAMES YOU TRUST

. . .ALL ARE GUARANTEED

THIS WEEK ONLY

TUESDAY
TOMORROW ONLY 10' til 4'

SPANISH

DANISH

French

WALNUT SET

. . . Soft Pecan

Built of Select Woods

EASY TERMS

Instant Credit

FREE BONUS GIFT

. . . Free Delivery

PAR. 5. By and through the use of the above–quoted statements and representations, and others of similar import and meaning but not expressly set out herein, separately and in connection with the oral statements and representations of respondent's salesmen to customers and prospective customers, respondent has represented, and is now representing, directly or by implication that:

1. Respondent is making a bona fide offer to sell the advertised merchandise at the prices and on the terms and conditions stated in the advertisements.

2. By and through the use of the words, "SALE," "SAVE," "EXTRA SAVINGS," and other words of similar import and meaning not set out specifically herein, respondent's merchandise may be purchased at special or reduced prices, and purchasers are thereby afforded savings from respondent's regular selling price.

3. The regular selling prices quoted in respondent's advertisements are the amounts at which the advertised merchandise has been sold or offered for sale by respondent for a substantial period of time in the recent, regular course of its business.

4. By and through the use of the words, "Huge Selection," "WE BOUGHT CARLOADS OF MERCHANDISE," and other words of similar import and meaning not set out specifically herein, the advertised merchandise is available in several different sets from which the prospective purchaser may choose.

5. By and through the use of the words, "IMMEDIATE AVAILABILITY," "NO WAITING," and other words of similar import and meaning not set out specifically herein, the advertised merchandise is readily available for sale in quantities sufficient to meet reasonably anticipated demands.

6. There are no charges in addition to the advertised purchase price of respondent's merchandise.

7. By and through the use of the words "GIANT FURNITURE VALUES," "GIGANTIC VALUE!," "NAMES YOU TRUST," and other words of similar import and meaning not specifically set out herein, the durability of the advertised merchandise exceeds reasonable requirements for normal everyday use for a reasonable period of time.

8. The advertised merchandise was guaranteed in every respect without conditions or limitations and would be continually serviced without charge for an unlimited period of time after the delivery of the advertised merchandise to the homes of purchasers.

9. The advertised offer was being made only for a limited period of time.

10. Purchasers of the advertised merchandise are afforded savings of $100 and more off the prices at which such merchandise is usually and customarily sold at retail.

11. By and through the use of the words, "DANISH," "French," "SPANISH," and other words of similar import and meaning not set out specifically herein, furniture sold by respondent is of a foreign origin.

12. By and through the use of the words, "Walnut Set," "Soft Pecan," "Built of select woods," and other words of similar import and meaning not set out specifically herein, furniture sold by respondent is of solid wood construction.

13. By and through the use of the words, "Instant Credit" and "Easy Terms," purchasers of respondent's merchandise are never refused credit and are granted easy credit terms without regard to their financial status or ability to pay.

14. Free merchandise and services will be given to all purchasers of respondent's advertised products.

PAR. 6. In truth and in fact:

1. The offers set out in respondent's advertisements are not bona fide offers to sell the advertised merchandise at the prices or on the

terms or conditions stated but are made for the purpose of obtaining leads to prospective purchasers.

2. Respondent's merchandise is not being offered for sale at special or reduced prices, and savings are not thereby afforded to their purchasers because of reductions from respondent's regular selling prices. In fact, respondent does not have regular selling prices, but the prices at which respondent's merchandise is sold vary from purchaser to purchaser.

3. The regular selling prices quoted in respondent's advertisements are not the respondent's regular selling prices but constitute fictitious higher prices upon which a deceptive sale comparison or similar offer may be based.

4. The advertised merchandise is not available in several different sets from which the prospective purchaser may choose. To the contrary, respondent has available only a very limited number of selections of the advertised merchandise.

5. All advertised merchandise is not readily available for sale in quantities sufficient to meet reasonably anticipated demands.

6. Respondent makes extra charges as applicable, such as service, finance and life insurance charges over and above the regular advertised price of their merchandise.

7. The advertised merchandise is not of a high quality or durability that exceeds reasonable requirements for normal everyday use for a reasonable period of time. In many instances, respondent sells advertised merchandise only under the express condition that such merchandise is not warranted for any particular use.

8. The advertised merchandise is not guaranteed by respondent and is not continuously serviced without charge for an unlimited period of time.

9. Respondent's advertised offer is not made for a limited period of time. The advertised merchandise is regularly advertised for the represented price or at another so-called reduced price over a period of time greater than the represented limitations.

10. Purchasers of respondent's merchandise advertised in conjunction with the phrase "Save Up To $100 and More," or terms of similar comparable import or meaning, did not realize savings of the stated percentage amount from the actual prices at which the merchandise so advertised was sold or offered for sale in good faith for a reasonably substantial period of time in the recent regular course of respondent's business.

11. Merchandise advertised in conjunction with the words, "DANISH," "French," or "SPANISH," or terms of comparable import or

meaning, is not of a foreign origin. The advertised merchandise is produced by domestic manufacturers.

12. Merchandise advertised in conjunction with the use of the phrases, "walnut set," "soft Pecan," "Built of select woods," or terms of similar comparable import or meaning, was not of solid wood construction. To the contrary, said phrases merely described the color of a stain finish applied to the exposed surfaces of the merchandise.

13. Purchasers of respondent's merchandise are not granted instant credit or easy credit terms by respondent, without regard to their financial status or ability to pay.

14. Respondent does not give free merchandise and services to all purchasers of its advertised products in accordance with its promises or offers. In many cases, respondent marks up the price of advertised products to include the cost of such gifts or services and frequently advertised merchandise is only given to purchasers who specifically request them when purchasing advertised products.

Therefore, the statements and representations set forth in Paragraphs Four and Five hereof were and are false, misleading and deceptive.

PAR. 7. In the course and conduct of its business and for the purpose of inducing the sale of its household furniture, respondent through the use of pictorial representations in various publications and T.V. commercials, represented directly or by implication that:

1. All of the furniture illustrated in the pictorial representation is being offered for sale at the advertised price.

2. All of the furniture illustrated in the pictorial representation is available for sale in unlimited quantities as a group.

3. Furniture illustrated in the pictorial representation may be purchased at special or reduced prices, and purchasers are thereby afforded savings from respondent's regular selling price.

PAR. 8. In truth and in fact:

1. Respondent offers only part of the furniture in the pictorial representation at the advertised price and makes extra changes as applicable for remaining furniture items in the pictorial representation.

2. All of the furniture in the pictorial representation is not available for sale in unlimited quantities as a group. To the contrary, respondent has available only a very limited number of the advertised groups of furniture.

3. Furniture illustrated in the pictorial representation is not being offered for sale at special or reduced prices, and savings are not afforded to purchasers because of reductions from respondent's regular selling prices. In fact, respondent does not have regular selling

prices, but the prices at which respondent's merchandise is sold vary from purchaser to purchaser.

Therefore, the representations set forth in Paragraph Seven hereinbefore, were, and are, false, misleading and deceptive.

PAR. 9. In the course and conduct of its business and for the purpose of inducing the sale of its furniture, respondent has maintained, and is now maintaining, in its salesrooms, floor models and displays of furniture being offered for sale, on the basis of which its customers select and order the furniture they purchase from respondent.

In this connection, respondent and its sales representatives have made, and are now making, numerous oral statements and representations to customers and prospective customers regarding the quality and durability of the furniture being offered for sale, the terms and conditions under which merchandise will be sold and delivered, and the services that will be provided by respondent.

Moreover, subsequent to making sales and deliveries, respondent and its employees have made, and are now making, numerous oral statements, representations and promises to their customers regarding the time and manner in which respondent will perform various adjustments, replacements and/or repairs.

PAR. 10. By and through the use of the floor models and furniture displays, together with the aforesaid oral statements, representations and promises made by respondent, its sales representatives and other employees, respondent has represented, and is now representing, directly or by implication, that:

1. Furniture sold by respondent will be delivered to the customer free from damages and defects.
2. Furniture which is delivered to purchasers with damages and/or defects will be repaired or replaced within a reasonable time.
3. Furniture which is delivered with damages and/or defects will be repaired or replaced to the satisfaction of the purchasers.
4. Furniture which is delivered to purchasers with damages and/or defects will be repaired or replaced in accordance with promises made to the purchasers by respondent.

PAR. 11. In truth and in fact:

1. In many instances, furniture sold by respondent is delivered to purchasers with damages and/or defects.
2. In many instances, furniture which is delivered to purchasers with damages and/or defects is not repaired or replaced within a reasonable time.
3. In many instances, furniture which is delivered to purchasers with damages and/or defects is not repaired or replaced to the satisfaction of the purchasers.

4. In many instances, furniture which is delivered to purchasers with damages and/or defects is not repaired or replaced in accordance with promises made to the purchasers by respondent's employees.

Therefore, the aforesaid acts, practices, statements and representations regarding respondent's merchandise and service as set forth in Paragraphs Nine and Ten were, and are, false, misleading and deceptive.

PAR. 12. In the further course and conduct of its aforesaid business, and in connection with the representations set forth in Paragraphs, Four, Five, Seven, Nine and Ten above, respondent in offering its furniture for sale has failed to disclose material facts relating to the veneered construction or to the use of plastics with simulated wood appearance in the manufacture of its merchandise.

The aforesaid failure to disclose such material facts to purchasers has the tendency and capacity to mislead or deceive such persons with respect to the utility, construction, composition, durability, design and grade of household furniture sold by respondent.

Therefore, respondent's failure to disclose such material facts was, and is, unfair, false, misleading and deceptive.

PAR 13. In the further course and conduct of its business, and in furtherance of a sales program for inducing the purchase of its furniture and appliances, respondent's salesmen or representatives have in many instances engaged in the following additional unfair, false, misleading and deceptive acts and practices:

1. They have obtained purchasers' signature on blank retail installment contracts and other instruments by making false and misleading representations and deceptive statements, including false and deceptive representations with respect to the nature and effect thereof, to induce purchasers to sign such instruments.

2. Through the use of false, misleading and deceptive statements, representations and practices set forth in Paragraphs Four through Twelve above, respondent or its representatives have been able to induce their customers into signing a contract upon initial contact without giving the customers sufficient time to carefully consider the purchase and consequence thereof.

3. They have failed to disclose certain material facts to purchasers, including but not limited to the fact that, at respondent's option, conditional sales contracts, promissory notes or other instruments of indebtedness executed by such purchasers in connection with their credit purchase agreements may be discounted, negotiated or assigned to a finance company or other third party to whom the purchaser is thereafter indebted and against whom defenses may not be available.

Therefore, the acts and practices, as set forth in Paragraph Thirteen hereof, were, and are, false, misleading and deceptive.

PAR. 14. In the course and conduct of its aforesaid business, and at all times mentioned herein, respondent has been, and is, in substantial competition, in commerce, with corporations, firms and individuals in the sale of merchandise of the same general kind and nature as that sold by respondent.

PAR. 15. The use by respondent of the aforesaid false, misleading and deceptive statements, representations, and acts and practices, has had, and now has, the capacity and tendency to mislead members of the purchasing public into the erroneous and mistaken belief that said statements and representations were, and are, true and complete, and into . he purchase of substantial quantities of respondent's products by reason of said erroneous and mistaken belief.

PAR. 16. The aforesaid acts and practices of respondent, as herein alleged, were and are all to the prejudice and injury of the public and of respondent's competitors and constituted, and now constitute, unfair methods of competition in or affecting commerce and unfair and deceptive acts and practices in or affecting commerce, in violation of Section 5 of the Federal Trade Commission Act.

COUNT II

Alleging violations of Section 5 of the Federal Trade Commission Act, the allegations of Paragraphs One and Two hereof are incorporated by reference in Count II as if fully set forth verbatim.

PAR. 17. In the course and conduct of its business, as aforesaid, respondent is engaging, and for some time last past has engaged, in the collection of debts allegedly due and owing to Hiken Furniture Company pursuant to contracts or other agreements relating to the purchase of respondent's merchandise.

PAR. 18. In attempting to induce payments of purportedly due or delinquent accounts, respondent and its representatives or agents have sent through the United States mail dunning letters, notices and similar instruments which contain false and misleading statements and representations.

Typical, but not all inclusive of such statements and representations are the following:

Unless we receive a payment within 5 days, we will be forced to file suit immediately thereafter. You will be charged all court costs and collection fees.

This is the final notice.

PAR. 19. By and through the use of the above-quoted statements and representations, and others of similar import and meaning but not specifically set forth herein, respondent has represented, directly or by implication, that:

1. Respondent has referred, is referring or will refer delinquent accounts to attorneys.
2. Failure to pay the amount claimed as owing within a stated period of time will result in immediate legal action.
3. Once judgment is entered against a debtor, it is impossible for the debtor to avoid payment thereof.
4. Respondent's organization has or maintains a separate legal department with qualified employees serving in this department.

PAR. 20. In truth and in fact:

1. Failure of an alleged debtor to remit money to respondent within time period(s) indicated does not in most instances result in the immediate reference of such matters to attorneys.
2. Failure of an alleged debtor to remit money to respondent within time period(s) indicated does not in most instances result in the immediate institution of legal action to effect payment.
3. It is possible to avoid payment of a judgment, once such is entered, in a matter involving a debt. For instance, resort to bankruptcy proceedings will often avoid the payment of at least part of a judgment. Also, the restrictions and exemptions placed on the collection of judgments make it possible in some instances to avoid the payment of at least part of a judgment.
4. Respondent does not have a separate legal department with qualified employees serving in this department.

Therefore, the statements and representations set forth in Paragraphs Nineteen and Twenty hereof were and are false, misleading and deceptive.

PAR. 21. The use by the respondent of the aforesaid false, misleading and deceptive statements, representations and practices has had, and now has, the tendency and capacity to mislead and deceive members of the public into the erroneous and mistaken belief that said statements and representations were, and are, true and to induce recipients thereof into the payment of alleged delinquent accounts by reason of the said erroneous and mistaken belief.

PAR. 22. The aforesaid acts and practices of respondent as herein alleged were, and are, all to the prejudice and injury of the public and respondent's competitors and constituted, and now constitute, unfair methods of competition in or affecting commerce, and unfair and deceptive acts and practices in or affecting commerce, in violation of Section 5 of the Federal Trade Commission Act.

COUNT III

Alleging violations of the Truth in Lending Act and the implementing regulation promulgated thereunder and of the Federal Trade Commission Act, the allegations of Paragraphs One and Two hereof are incorporated by reference in Count III as if fully set forth verbatim.

PAR. 23. In the ordinary course and conduct of its business, as aforesaid, respondent regularly extends, and for some time last past has regularly extended consumer credit, as "consumer credit" is defined in Regulation Z, the implementing regulation of the Truth in Lending Act, duly promulgated by the Board of Governors of the Federal Reserve System.

PAR. 24. Subsequent to July 1, 1969, in the ordinary course of business as aforesaid, and in connection with its credit sales, as "credit sale" is defined in Regulation Z, respondent has caused and is causing customers to execute a binding "Retail Installment Contract" hereinafter referred to as the "Installment Contract." Respondent does not provide these customers with any other credit cost disclosures.

By and through the use of the Installment Contracts, respondent:

1. Induced certain customers to sign installment contracts in blank form. Respondent has subsequently filled in the blank spaces and frequently failed to give those customers a completed copy, thereby failing to furnish those customers any cost or credit disclosures prior to the consummation of the contract as required by Section 226.8(a) of Regulation Z in the manner and form prescribed by Sections 226.8(b) and (c) of Regulation Z.

2. Failed to meet the requirements of Section 226.8(b)(7) of Regulation Z as the contract provides for the right of payment of the full amount due and "under certain conditions" to obtain a partial refund of the finance charge, without further disclosing the "certain conditions" under which prepayment could be made and a partial refund of the finance charge be obtained.

3. Failed to accurately disclose the date on which the finance charge begins to accrue as prescribed by Section 226.8(b)(1) of Regulation Z.

4. Failed to accurately state the "annual percentage rate," as prescribed by Section 226.8(b)(2) of Regulation Z.

5. Failed to disclose the total of payments as prescribed by Section 226.8(b)(3) of Regulation Z.

6. Failed to accurately disclose the number, amount and due dates, or periods of payments, scheduled to repay the indebtedness, as prescribed by Section 226.8(b)(3) of Regulation Z.

7. Failed to state the "unpaid balance of cash price," as prescribed by Section 226.8(c)(3) of Regulation Z.

8. Failed to disclose the amount financed, as required by Section 226.8(c)(7) of Regulation Z.

9. Failed to disclose the "deferred payment price," as prescribed by Section 226.8(c)(8)(ii) of Regulation Z.

10. Failed to include in the finance charge, charges or premiums for fire risk of loss insurance, written in connection with credit transactions when the customer was not given a clear, conspicuous, and specific written statement setting forth the cost of the insurance if obtained from or through respondent and stating that the customer may choose the person through which the insurance is to be obtained as prescribed by Section 226.4(a)(6) of Regulation Z.

11. Failed to include in the finance charge, charges or premiums for credit life, accident, health or loss of income insurance, written in connection with credit transactions when the customer has not given a specific dated and separately signed affirmative written indication of his desire for such coverage as prescribed by Section 226.4(a)(5)(ii) of Regulation Z.

PAR. 25. Pursuant to Section 103(q) of the Truth in Lending Act, respondent's aforesaid failures to comply with the provisions of Regulation Z constituted violations of that Act and, pursuant to Section 108 thereof, respondent has thereby violated the Federal Trade Commission Act.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Chicago Regional Office proposed to present to the Commission for its consideration, and which, if issued by the Commission, would charge respondent with violation of the Federal Trade Commission Act; and

The respondent and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted and executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following orders:

1. Respondent Hiken Furniture Company is a corporation organized, existing and doing business under and by virtue of the laws of the State of Illinois, with its office and principal place of business located at 218 West Main St., Belleville, Illinois.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER I

It Is ordered, That respondent Hiken Furniture Company, a corporation, its successors and assigns, and its officers, agents, representatives and employees, directly or through any corporation, subsidiary, division or any other device in connection with the purchasing, advertising, offering for sale, sale and distribution of furniture and appliances, or any other products, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

1. Using, in any manner, a sales plan, scheme, or device wherein false, misleading, or deceptive statements or representations are made in order to obtain leads or prospects for the sale of merchandise.

2. Making representations, directly or indirectly, orally or in writing, purporting to offer merchandise or services for sale when the purpose of the representations is not to sell the offered merchandise or services but to obtain leads or prospects for the sale of other merchandise or services at higher prices.

3. Discouraging in any manner the purchase of any merchandise or services which are advertised or offered for sale as part of a scheme to sell other merchandise.

4. Failing to maintain and produce for inspection and copying for a period of three years adequate records to document for the entire period during which each advertisement was run and for a period of six weeks after the termination of its publication in press or broadcast media:

a. the cost of publishing each advertisement including the preparation and dissemination thereof;

b. the volume of sales made of the advertised product or service at the advertised price;

c. a computation of the net profit from the sales of each advertised product or service at the advertised price, based upon respondent's normal method of computation.

5. Using the words "Sale," or "Save," "Extra Savings," or any other words of similar import or meaning not set forth specifically herein, unless the immediately preceding price at which bonafide sales have been made of the merchandise being offered for sale is disclosed or can be readily ascertained by disclosure of the stated dollar or percentage price and the price of said merchandise constitutes a recent reduction, in an amount not so insignificant as to be meaningless, from the immediately preceding price or unless a disclosure is made that such merchandise was offered for sale at the immediately preceding price in the recent regular course of respondent's business, and that no sales were made at that price or any other price in the recent past.

6. (a) Representing, directly or indirectly, orally or in writing, that by purchasing any of respondent's merchandise, customers are afforded savings amounting to the difference between respondent's stated price and respondent's former price unless the former price is respondent's immediately preceding price for the advertised merchandise and bona fide sales have been made by respondent at that price in the recent past or unless a disclosure is made that said merchandise was offered for sale at the former price for a reasonably substantial period of time in the recent regular course of respondent's business and that no sales were made at that price or at any other price in the recent past.

(b) Representing, directly or indirectly, orally or in writing that by purchasing any of the respondent's merchandise, customers are afforded savings between respondent's stated price and a compared price for said merchandise in respondent's trade area unless respondent's merchandise and the nature of the compared price are explicitly identified in advertising and at the point of sale through the use of shelf tags or similar means and such merchandise is generally available in principal retail outlets in the trade area at the compared price or some higher price.

(c) Representing, directly or indirectly, orally or in writing, that by purchasing any of respondent's merchandise, customers are afforded savings amounting to the difference between respondent's stated price and a compared value price for comparable merchandise unless the compared value price is explicitly identified in advertising and at the point of sale through the use of shelf tags or similar means and respondent has in good faith conducted a market survey or obtained a similar representative sample of prices for comparable merchandise of like grade and quality in its trade area to establish that the principal retail outlets in the trade area regularly sell comparable merchandise of like grade and quality at the compared value price in the regular course of their business.

7. Failing to maintain and produce for inspection or copying, for a period of three years, adequate records (a) which disclose the facts upon which any savings claims, sale claims and other similar representations are set forth in Paragraphs Five and Six of this order are based, and (b) from which the validity of any savings claims, sale claims, and similar representations can be determined.

8. Representing, directly or indirectly, orally or in writing, that respondent has a "Huge Selection," "Carloads," or any given number of furniture suites unless respondent has the stated huge selection or number of furniture suites available for immediate sale and delivery; or misrepresenting in any manner the colors, style, kind or quantity of furniture in stock and available for sale or delivery.

9. Representing, directly or indirectly, orally or in writing, the immediate availability of any merchandise for sale when such merchandise is not in stock and available in quantities sufficient to meet reasonably anticipated demands for sale to the public at or below the advertised price for the period in which the prices are advertised to be effective.

10. Failing to make full disclosure either in its advertising or at the time of sale and prior to consummation of the sale that in addition to the price quoted in respondent's advertising, certain other charges, as applicable, are made, such as, delivery, set-up or assembly, service, and warranty charges.

11. Failing to disclose clearly and conspicuously within each advertisement for an advertised product each reservation, if any, as to suitability or durability of such advertised product for reasonable usage by the customers who may buy such product or service.

12. Representing, directly or by implication, that any of respondent's offers to sell merchandise are limited as to time or restricted or limited in any other manner, unless such represented limitations or restrictions are actually in force and in good faith adhered to.

13. Using the terms "Danish," "French," or "Spanish," or any other unqualified terms of similar import or meaning not set forth specifically herein, orally or in writing, to describe respondent's furniture when such furniture is of domestic origin, unless a clear and conspicuous disclosure is made in advertising and on the furniture that such furniture was manufactured in the United States by means of

such statements as "Made In U.S.A." or "manufactured by" followed by the name and address of the domestic manufacturer.

14. Representing, directly or indirectly, orally or in writing, that the respondent's merchandise is "soft pecan," "walnut," or using any other terms of comparable import or meaning not set forth specifically herein, to describe respondent's furniture, unless a clear and conspicuous disclosure is made in advertising and on furniture that such terms are merely descriptive of the color and/or grain design or other simulated finish that is applied to the exposed surfaces of such furniture.

15. Using any wood names or any names that suggest wood, orally or in writing, to describe any materials simulating wood in respondent's furniture, unless a clear and conspicuous disclosure is made in advertising and on the furniture that such wood names are merely descriptive of the color and/or grain design or other simulated finish that is applied to the exposed surfaces of such furniture.

16. Representing, directly or indirectly, orally or in writing, that purchasers of respondent's merchandise are granted easy or instant credit terms, by respondent; or misrepresenting in any manner, the amount, type, extent of any other facet of the credit terms respondent arranges or may arrange for its purchasers.

17. Using the word "free" or any other word or words of similar import or meaning in connection with the sale, offering for sale or distribution of respondent's merchandise or services in advertisements or other offers to the public, as descriptive of an article of merchandise or service:

(a) When all the conditions, obligations, or other prerequisites to the receipt and retention of the "free" article of merchandise or service offered are not clearly and conspicuously set forth at the outset so as to leave no reasonable probability that the terms of the offer might be misunderstood.

(b) When, with respect to any article of merchandise or service required to be purchased in order to obtain the "free" article or service, the offerer either (i) increases the ordinary and usual price of such merchandise or service or (ii) reduces the quality or (iii) reduces the quantity or size thereof.

18. Offering gift merchandise to persons complying with certain conditions unless, in every instance, such merchandise is given to the persons complying with such conditions.

19. Using pictorial representations of two or more items of furniture in conjunction with a stated price when all of the furniture in the pictorial representations is not being offered at the stated price, unless a disclosure is made in immediate conjunction and with equal

prominence that all of the illustrated furniture is not being offered at the stated price and that an additional charge is made for certain items that are clearly identified in the illustrations.

20. Offering merchandise for sale by means of any form of pictorial advertisement when such merchandise is not in stock and available in quantities sufficient to meet reasonably anticipated demands for sale to the public at or below the advertised price for the period in which the prices are advertised.

21. Failing to make a clear and conspicuous disclosure on furniture, or on a tag or label prominently attached thereto, that veneers, plastics or other materials having the appearance of wood, leather, slate or marble have been used in the manufacture of such merchandise; or failing to make a clear and conspicuous disclosure of any material facts relating to the true composition of furniture where materials or products that simulate other materials or products are used in the manufacture of such furniture.

22. Failing to inform, orally, all customers at the time of sale and provide in writing on the fact of all order forms, sales contracts and invoices executed by customers with such conspicuousness and clarity as is likely to be read and understood, that, if furniture and/or appliances are delivered in a defective or damaged condition, the customer has the right to have such merchandise replaced or repaired with no additional cost to the customer by notifying respondent, in writing, within ten (10) days of the receipt of such damaged or defective merchandise and to cancel the contract and obtain a refund of all monies where respondent refuses or fails to make such replacement or repairs; *provided, however*, that the provisions of Paragraphs 22 and 23 of the order shall not apply to merchandise sold "as is," conspicuously designated as such on order forms, sales contracts and invoices executed by the customers who have knowledge of damage to, or defects in particular merchandise and have given written consent to purchasing same in its stated form.

23. Failing to replace or repair merchandise delivered in a defective or damaged condition with no additional cost to customers who have requested replacement or repair in writing within ten (10) days from the date of actual delivery of such merchandise, such replacement or repair to be fully, satisfactorily and promptly performed in accordance with Paragraph 24 of this Order I; *provided, however*, that in lieu of replacement and repair of defective or damaged merchandise, respondent may cancel the contract with immediate refund of all monies to customers who have requested such replacement or repair in writing. In cases where replacement or repairs have been made by respondent, the customer may cancel the contract with a refund of all

monies by notification to respondent in writing within ten (10) days from the date of actual delivery or redelivery of any replacement or repaired merchandise that is itself defective or damaged.

24. Failing on receipt of a written notice of defective or damaged merchandise to investigate such complaints forthwith and complete all repairs within three (3) weeks from the date of such notice or to make full replacements within forty (40) days of the receipt of such notice. In all other cases of actual delivery or redelivery or any replacement or repaired merchandise that is itself defective or damaged, respondent shall refund immediately all monies to customers who have requested contract cancellation in writing, as provided for in this order, or obtain the voluntary written consent of the customer for replacement or repair within one (1) week of the receipt of the customer's request for cancellation; shall complete all repairs pursuant to a written consent for repairs, within two (2) weeks from the date of such written consent and shall make full replacements, pursuant to a written consent for replacement, within thirty (30) days from the date of such written consent.

25. Failing to notify the customer, orally and in writing, and at least five (5) business days prior to the scheduled completion date, that respondent is unable to complete repairs or replacement within the time specified by this order and to cancel the contract with a full refund of all monies to the customer within one week, or in lieu thereof and at the option of the customer, to obtain the customer's voluntary written consent for an extension of the date set for completion, which shall be a date by which respondent actually expects to complete performance.

26. Failing to maintain and produce for inspection or copying, for a period of two (2) years, adequate records which disclose the facts pertaining to the receipt, handling and disposition of each and every written communication from a customer requesting contract cancellation, refund, replacement or repair.

27. Failing, if the respondent and a customer are unable to agree upon a settlement of any controversy involving the delivery or repair of any damaged or defective furniture, appliances, or other merchandise, or the failure to replace or repair such damaged or defective merchandise or to make cancellations with refunds with respect thereto, then, at the option of the customer, such customer shall have the right to submit the issue to an impartial arbitration procedure entailing no mandatory administative cost or filing fee to the consumer, which shall be conducted in accordance with the arbitration procedures annexed to this order, as Appendix "A", and the procedures

for arbitration adopted in Appendix "A" are to be considered as incorporated within the terms of this order.

28. Failing to comply with and abide by any award or decision rendered pursuant to the arbitration procedures of Paragraph 27.

29. Preventing arbitration pursuant to any provision of this order by reason of having obtained a default judgment against any customer in an action for money allegedly due the respondent or its assignees.

30. Failing to provide adequate notification to customers of their right to submit such controversy to arbitration or failing to incorporate the following statement on the face of all sales contracts with such conspicuousness and clarity as is likely to be read and understood by customers.

NOTICE

Any controversy arising out of or relating to this contract involving the delivery or repair of any damaged or defective furniture, appliances or other merchandise, or the failure to replace or repair such damaged or defective merchandise or to make cancellations with refunds with respect thereto shall be settled, at the option of the customer, by arbitration. Such arbitration shall be conducted in accordance with Arbitration Rules of the Arbitration Tribunal of the Better Business Bureau of Greater St. Louis, Inc., whose offices are located at 915 Olive Street, Fourth Floor, St. Louis, Missouri 63101, telephone (314)241-3100. Under Missouri and Illinois law, arbitration, if undertaken, is legally binding and final.

31. Failing to change the instructions, contained in the Notice set forth in Order I, Paragraph 30 as to how to secure arbitration if circumstances require.

32. Inducing or causing purchasers or prospective purchasers of respondent's products, installations or services to sign blank or partially filled in completion certificates or other legal instruments or documents; or misrepresenting, in any manner, the true nature or effect of such legal instruments or documents.

33. Contracting for any sale whether in the form of trade acceptance, conditional sales contract, promissory note, or otherwise which shall become binding on the buyer prior to midnight of the third day, excluding Sundays and Legal holidays, after the date of execution.

34. Failing to furnish the buyer with a fully completed receipt or copy of any contract pertaining to such sale at the time of its execution, which is in the same language, *e.g.*, Spanish, as that principally used in the oral sales presentation and which shows the date of the transaction and contains the name and address of the seller, and in immediate proximity to the space reserved in the contract for the signature of the buyer or on the front page of the receipt if a contract

is not used and in bold face type of a minimum size of 10 points, a statement in substantially the following form:

YOU, THE BUYER, MAY CANCEL THIS TRANSACTION AT ANY TIME PRIOR TO MIDNIGHT OF THE THIRD BUSINESS DAY AFTER THE DATE OF THIS TRANSACTION. SEE THE ATTACHED NOTICE OF CANCELLATION FORM FOR AN EXPLANATION OF THIS RIGHT.

35. Failing to furnish each buyer, at the time he signs the sales contract or otherwise agrees to buy consumer goods or services from the seller, a completed form in duplicate, captioned "NOTICE OF CANCELLATION," which shall be attached to the contract or receipt and easily detachable, and which shall contain in ten point boldface type the following information and statements in the same language, *e.g.*, Spanish, as that used in the contract:

NOTICE OF CANCELLATION

(enter date of transaction)
(date)

YOU MAY CANCEL THIS TRANSACTION, WITHOUT ANY PENALTY OR OBLIGATION, WITHIN THREE BUSINESS DAYS FROM THE ABOVE DATE.

IF YOU CANCEL, ANY PROPERTY TRADED IN, ANY PAYMENTS MADE BY YOU UNDER THE CONTRACT OR SALE, AND ANY NEGOTIABLE INSTRUMENT EXECUTED BY YOU WILL BE RETURNED WITHIN 10 BUSINESS DAYS FOLLOWING RECEIPT BY THE SELLER OF YOUR CANCELLATION NOTICE, AND ANY SECURITY INTEREST ARISING OUT OF THE TRANSACTION WILL BE CANCELLED.

IF YOU CANCEL, YOU MUST MAKE AVAILABLE TO THE SELLER AT YOUR RESIDENCE, IN SUBSTANTIALLY AS GOOD CONDITION AS WHEN RECEIVED, ANY GOODS DELIVERED TO YOU UNDER THIS CONTRACT OR SALE; OR YOU MAY IF YOU WISH, COMPLY WITH THE INSTRUCTIONS OF THE SELLER REGARDING THE RETURN SHIPMENT OF THE GOODS AT THE SELLER'S EXPENSE AND RISK.

IF YOU DO MAKE THE GOODS AVAILABLE TO THE SELLER AND THE SELLER DOES NOT PICK THEM UP WITHIN 20 DAYS OF THE DATE OF YOUR NOTICE OF CANCELLATION, YOU MAY RETAIL OR DISPOSE OF THE GOODS WITHOUT ANY FURTHER OBLIGATION. IF YOU FAIL TO MAKE THE GOODS AVAILABLE TO THE SELLER, OR IF YOU AGREE TO RETURN THE GOODS TO THE SELLER AND FAIL TO DO SO, THEN YOU REMAIN LIABLE FOR PERFORMANCE OF ALL OBLIGATIONS UNDER THE CONTRACT.

TO CANCEL THIS TRANSACTION, MAIL OR DELIVER A SIGNED AND DATED COPY OF THIS CANCELLATION NOTICE OR ANY OTHER WRITTEN NOTICE, OR SEND A TELEGRAM TO ______________, AT *(address of seller's place of business)*; NOT LATER THAN MIDNIGHT OF *(Date)*.

I HEREBY CANCEL THIS TRANSACTION.

(Date)

(Buyer's Signature)

36. Failing, before furnishing copies of the "Notice of Cancellation" to the buyer, to complete both copies by entering the name of the seller, the address of the seller's place of business, the date of the transaction, and the date, not earlier than the third business day following the date of the transaction, by which the buyer may give notice of cancellation.

37. Including in any sales contract or receipt any confession of judgment or any waiver of any of the rights to which the buyer is entitled under this order including specifically his right to cancel the sale in accordance with the provisions of this order.

38. Failing to inform each buyer orally, at the time he signs the contract or purchases the goods or services, of his right to cancel.

39. Failing or refusing to honor any valid notice of cancellation by a buyer and within ten (10) business days after the receipt of such notice, to (a) refund all payments made under the contract or sale; (b) return any goods or property traded in, in substantially as good condition as when received by the seller; (c) cancel and return any negotiable instrument executed by the buyer in connection with the contract or sale and take any action necessary or appropriate to terminate promptly any security interest created in the transaction.

40. Negotiating, transferring, selling, or assigning any note or other evidence of indebtedness to a finance company or other third party prior to midnight of the fifth business day following the day the contract was signed or the goods or services were purchased.

41. Failing, within ten (10) business days of receipt of the buyer's notice of cancellation, to notify him whether the seller intends to repossess or to abandon any shipped or delivered goods.

ORDER II

It is further ordered, That respondent Hiken Furniture Company, a corporation, its successors and assigns, and its officers, agents, representatives and employees, directly or through any corporation, subsidiary, division or any other device, in connection with the collection of, or attempt to collect, accounts in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

1. Representing, or causing to be represented by any means, directly or indirectly, that respondent has instructed, is instructing, or will instruct an attorney to file suit against an alleged debtor unless the alleged debt is immediately paid in full or a specified amount is

paid thereon unless the respondent has already instituted the aforesaid suit, or do so in fact, if the alleged debt is not immediately paid in full or the specified amount is not paid thereon.

2. Representing by any means, directly or indirectly, that:

(a) legal action has been taken against the debtor; or

(b) legal action is being taken against the debtor; or

(c) legal action will be taken against the debtor unless the respondent has already instituted said legal action, or does so in fact, if the alleged debt is not immediately paid in full or the specified amount is not paid thereon.

3. Informing a debtor of a creditor's right after judgment without disclosing at the same time that no judgment may be entered against the debtor unless the debtor has first been given notice and an opportunity to appear and defend himself in a court of law.

4. Representing, directly or indirectly, by any means to a debtor that it is impossible to escape a judgment.

5. Failing to give notification of a commencement of legal action by respondent against customer by mailing a summons and complaint to such customer's last known address, and failing to obtain from the post office a certificate of such mailing. Such notice shall be in addition to any other notification or service required by law, practice or custom. Such summons and complaint to be sent by first class mail by respondent or its attorney with instructions on the face of the envelope "Do not forward. Address Correction Requested". In the event that such mail is returned as undeliverable by the Post Office or if the residence address of the defendant is unknown, the summons is to be mailed to the customer, care of the employer or place of employment of the customer if known, in a sealed envelope not indicating on the outside thereof, directly or indirectly by the return address or otherwise, that the communication is from an attorney or concerns an alleged debt.

ORDER III

It is further ordered, That respondent Hiken Furniture Company, a corporation, its successors and assigns, and its officers, agents, representatives and employees, directly or through any corporation, subsidiary, division or other device, in connection with any extension of consumer credit, or any advertisement to aid, promote or assist directly or indirectly any extension of consumer credit, as "consumer credit" and "advertisement" are defined in Regulation Z (12 CFR 226) of the Truth in Lending Act (Pub. Law 90–321, 15 U.S.C. 1601, *et seq.*), do forthwith cease and desist from:

1. Failing to furnish to the customer, before the transaction is

consummated, a duplicate of the instrument or other statement containing the disclosures required by Section 226.8 of Regulation Z, as required by Section 226.8(a) of Regulation Z.

2. Failing to disclose the conditions entitling a customer to a partial refund of the finance charge as required by Section 226.8(b)(7) of Regulation Z.

3. Failing to accurately disclose the date on which the finance charge begins to accrue, as prescribed by Section 226.8(b)(1) of Regulation Z.

4. Failing to accurately state the "annual percentage rate," as prescribed by Section 226.8(b)(2) of Regulation Z.

5. Failing to disclose the "total of payments," as prescribed by Section 226.8(b)(3) of Regulation Z.

6. Failing to accurately disclose the number, amount, and due dates, or periods of payment, scheduled to repay the indebtedness, as prescribed by Section 226.8(b)(3) of Regulation Z.

7. Failing to state the "unpaid balance of cash price," as prescribed by Section 226.8(c)(3) of Regulation Z.

8. Failing to disclose the "amount financed," as prescribed by Section 226.8(c)(7) of Regulation Z.

9. Failing to disclose the "deferred payment price," as prescribed by Section 226.8(c)(8)(ii) of Regulation Z.

10. Failing to itemize and include in the finance charge for purposes of disclosure of the finance charge and computation of the annual percentage rate, any and all charges for risk of loss insurance unless the customer was given a clear, conspicuous and specific written indication of the cost of such insurance coverage from respondent and stating that the customer may choose the source through which the insurance is to be obtained as prescribed by Section 226.4(a) (6) of Regulation Z.

11. Failing to itemize and include in the finance charge, for purposes of disclosure of the finance charge and computation of the annual percentage rate, any and all charges or premiums for credit life, accident, or health insurance unless respondent has obtained a specific dated and separately signed affirmative written indication of the customer's desire for such insurance coverage as prescribed by Section 226.4(a) (5)(ii) of Regulation Z.

12. Failing, in any consumer credit transaction or advertisement, to make all disclosures determined in accordance with Sections 226.4 and 226.5 of Regulation Z, in the manner, form and amount required by Sections 226.6, 226.7, 226.8, 226.9 and 226.10 of Regulation Z.

It is further ordered, That respondent shall forthwith cease and desist from representing, orally, directly or by implication that respondent offers a guarantee or warranty of any kind and from offering a warranty of any kind in writing that does not conform to all the requirements of the Magnuson-Moss Warranty — Federal Trade Commission Improvement Act of 1975, 15 USC 2301.

It is further ordered, That for a period of one year respondent post in a prominent place in each salesroom or other area wherein respondent sells furniture or other products and services a copy of this cease and desist order with a notice that any customer or prospective customer may receive a copy on demand.

It is further ordered, That respondent forthwith distribute a copy of this order to each of its operating divisions or departments.

It is further ordered, That respondent prominently display the following notice in two or more locations in that portion of respondent's business premises most frequented by prospective customers, and in each location where customers normally sign consumer credit documents or other binding instruments. Such notice shall be considered prominently displayed only if so positioned as to be easily observed and read by the intended individuals:

NOTICE TO CREDIT CUSTOMERS

IF THE DEALER IS FINANCING OR ARRANGING THE FINANCING OF YOUR PURCHASE, YOU ARE ENTITLED TO CONSUMER CREDIT COST DISCLOSURES AS REQUIRED BY THE FEDERAL TRUTH IN LENDING ACT. THESE MUST BE PROVIDED TO YOU IN WRITING BEFORE YOU ARE ASKED TO SIGN ANY DOCUMENT OR OTHER PAPERS WHICH WOULD BIND YOU TO SUCH A PURCHASE.

This notice required by order of the Federal Trade Commission.

It is further ordered, That no provision of this order shall be construed in any way to annul, invalidate, repeal, terminate, modify or exempt respondent from complying with agreements, orders or directives of any kind obtained by any other agency or acts as a defense to actions instituted by municipal or state regulatory agencies. No provision of this order shall be construed to imply that any past or future conduct of the respondent complies with the rules and regulations of, or the statutes administered by the Federal Trade Commission.

It is further ordered, That respondent deliver a copy of this order to cease and desist to all present and future personnel of respondent engaged in the consummation of any consumer credit transaction or in any aspect of preparation, creation or placing of advertising, and to all personnel of respondent responsible for the sale or offering for sale of all products covered by this order, and that respondent secure a signed statement acknowledging receipt of said order from each person.

It is further ordered, That respondent, for a period of one year from the effective date of this order, shall furnish each newspaper or other advertising medium which is utilized by the respondent to obtain leads for the sale of merchandise, or to advertise, promote, or sell merchandise, with a copy of the Commission's News Release setting forth the terms of this order.

It is further ordered, That respondent notify the Commission at least 30 days prior to any proposed change in the respondent corporation such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance obligations arising out of the order.

It is further ordered, That in the event respondent merges with another corporation or transfers all or a substantial part of its business or assets to any other corporation or to any other person, said respondent shall require such successor or transferee to file promptly with the Commission a written agreement to be bound by the terms of this order; provided that if said respondent wishes to present to the Commission any reasons why said order should not apply in its present form to said successor or transferee, it shall submit to the Commission a written statement setting forth said reasons prior to the consummation of said successions or transfer.

It is further ordered, That the respondent herein shall within sixty (60) days after service upon it of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which it has complied with this order.

APPENDIX "A"

CONSUMER ARBITRATION RULES

DEFINITIONS

A. *Arbitration* is the process by which two or more parties select and authorize an impartial party or panel to resolve their dispute.

B. *Consumer disputes* are any disagreements between respondent and his customer involving the delivery or repair of any damaged or defective furniture, appliances, or other merchandise, or the failure to replace or repair such damaged or defective merchandise or to make cancellations with refunds with respect thereto. If during the course of any proceeding conducted pursuant these Rules, it appears to the Arbitrator that the issues before him do not coincide with this definition, he is authorized to suspend the hearing permanently, narrow the issues to those which fall within this definition, or take whatever other action is deemed necessary.

C. *Administrator* refers to the Better Business Bureau of Greater St. Louis, Inc.

D. *Parties* to arbitration are those persons necessary to resolve a dispute, usually the businessman and his customer.

E. *Arbitrator* is the individual or panel which makes the final decision or award.

APPLICATION OF RULES

These Rules shall apply to consumer disputes submitted to the Administrator for settlement by arbitration. The Parties shall be deemed to have adopted these Rules whenever they have agreed in writing to arbitrate their dispute. These rules and any amendment thereof shall apply to the form obtaining at the time the arbitration is initiated.

INITIATING ARBITRATION

If it appears that efforts to resolve a dispute informally have been exhausted, the Bureau may suggest or the Parties may request that the dispute be arbitrated. The Administrator will then prepare an Arbitration Agreement, on which the issues in dispute are listed, and transmit an identical Agreement to both Parties. If the Parties agree with the listed issues and further agree to be bound by arbitration, they will sign the Agreement and return it to the Administrator within five (5) days after receipt. If either Party disagrees with the issues presented, he shall return a corrected version of the issues to the Administrator. The Administrator shall resolve any conflict of issues and, if necessary, send amended Arbitration Agreements for signature by the Parties. Failure to return a signed Arbitration Agreement will be considered as a rejection of arbitration. Upon receipt of signed Agreements from the Parties, the Administrator shall commence procedures to arbitrate a dispute pursuant to these Rules.

The Administrator may require the posting of a nominal performance bond by either of the Parties to assure their presence at the hearing. Such a bond, if posted, shall be returned to the Party when he presents himself at the hearing.

SELECTION OF ARBITRATOR

The Administrator shall maintain a pool of volunteers from which the Arbitrator shall be selected. This pool of volunteers should reflect membership of the total community. The following methods of selection Arbitrators may be used:

A. The Single Arbitrator

A single Arbitrator shall be used in all cases where the Arbitrator has been selected and agreed upon by the Parties from the established pool of Arbitrators. Upon receipt of written Agreements to binding arbitration by the Parties, the Administrator shall provide the Parties with an identical list of five Arbitrators chosen from the pool, together with brief biographies of each. Each Party shall have five (5) days after receipt of this list to cross off names of those deemed unacceptable to him and rank the remaining names in descending order of preference, placing #1 after name of first choice, etc. The Administrator shall select an Arbitrator from the top three choices of the Parties. If preferences of the Parties do not overlap, the Administrator may either send the Parties a new list of Arbitrators or set up a panel, described in Section B., below.

B. Three-Man Panel

Upon demand of either Party to a dispute involving amounts exceeding $1,000.00 or when the Parties cannot agree upon a single Arbitrator, each Party selects from the pool an Arbitrator representing his first choice. The two Arbitrators so selected shall select from the pool a third Arbitrator who has not been previously rejected by either Party. The person so selected shall serve as chairman and convenor of the panel.

FACILITIES AND COSTS

Facilities for the holding of hearings and maintenance of records shall be provided by the Administrator. Cost of stenographic services, record of proceedings and individual witness fees shall be borne by the respondent. The Administrator will endeavor to provide a panel of expert witnesses and testing laboratories willing to donate services.

COMMUNICATION AND SERVING OF NOTICES

All correspondence should be sent by mail to the Administrator. There shall be no direct communication between the Parties and the Arbitrator regarding the dispute, except at the hearing and in the presence of the other Party, or with the other Party's written permission. All correspondence from the Parties to the Arbitrator and vice versa shall be sent through the Administrator. Any Party agreeing to arbitration pursuant to those Rules shall be deemed to have consented that any notices or other communication relevant to arbitration proceedings may be served by mail addressed to the Party or his attorney at his last known address. The Administrator shall notify the Parties of the date, time and place of the arbitration hearing and shall forward to the Parties a copy of the Award by registered mail, return receipt requested.

NOTICE OF APPOINTMENT

Notice of Appointment shall be mailed to the Arbitrator by the Administrator along with a copy of these Rules. The signed appointment form together with disclosures of any relationships to Parties shall be filed with the Administrator prior to the opening of the first hearing.

DISCLOSURE BY ARBITRATORS: FILLING VACANCIES

Any person selected to serve as an Arbitrator shall divulge, in his signed acceptance of appointment any financial, competitive, professional, family, or social relationship, however remote, with the Parties to the dispute or disputes he is assigned to arbitrate. All doubts should be resolved in favor of disclosure. Any such disclosures shall be transmitted to the Administrator who shall provide them to the Parties with a waiver/objection form. If a Party objects or if an Arbitrator is unable or unwilling to serve, the Administrator shall assist the Parties, pursuant to Section 5 of these Rules, in selecting or appointing a replacement.

REPRESENTATION BY COUNSEL

A Party may (but need not) be represented by counsel. A corporation may be represented by any officer or employee designated by the corporation. The Administrator and the opposing Party shall be furnished the name and address of any attorney for any Party at least five (5) days prior to the date of the hearing set before the Arbitrator.

HEARING DATES; NOTICES; WAIVER OF NOTICE

Upon acceptance of an Arbitrator, the Administrator shall, within three days, establish a date, time and place for the oral hearing, with due regard for the convenience of the Parties and with the agreement of the Arbitrator. Once determined, this information shall be communicated to the Parties at least seven days in advance of the date set for the hearing, utilizing the Notice of Hearing Form. Parties objecting to the date, time or location designated should promptly notify orally and in writing the Administrator or otherwise be deemed to have waived such objections. Appearance of the Party at hearings shall automatically constitute waiver of notice.

WAIVER OF ORAL HEARINGS

The Parties may agree in writing to waive oral hearings and to permit arbitration based on submission of written arguments and documentary evidence. Where oral hearings are waived, the Arbitrator shall determine the deadlines for submitting evidence. In such instances, the date for the Award shall be fixed at 10 days after receipt of all evidence.

INSPECTION BY ARBITRATOR

At the initiation of arbitration, either Party may request an inspection or a hearing at a site appropriate for inspection. The Arbitrator has the absolute discretion to inspect the product or premises involved. If the inspection is to be conducted separately from the hearing, the Administrator shall provide notice to the Parties and invite their presence. The Administrator shall also arrange for the presence of a technical expert at the inspection at the discretion of the Arbitrator. If possible, inspections should be conducted prior to the hearing.

ATTENDANCE AT PROCEEDINGS

Unless otherwise agreed by the Parties in writing only those persons party to or having a direct interest in the dispute are entitled to attend hearings. The Arbitrator shall have the discretion to require any witness to absent himself from the hearing room when the Arbitrator deems his presence to be unnecessary or undesirable.

ABSENCE OF A PARTY

Arbitration hearings may proceed in the absence of any Party who, after due notice of the hearing, fails to appear, but such absence shall not be the basis for a default judgment. Rather, the attending Party shall submit evidence and the Arbitrator may render an Award based thereon.

TRANSCRIPT OF HEARING

The Administrator shall provide stenographic services or otherwise record the proceedings upon the request of any Party, provided, however, that the cost of such services be borne by the requesting Party and that all Parties be provided access to such record. In all cases, the Arbitrator shall see that a Record of Hearing Form is completed at the close of each hearing.

INTERPRETERS

The Administrator shall provide without cost an Interpreter when any Party expresses the need for such and when the Arbitrator deems it necessary.

OATHS

The Arbitrator, the Parties, and any witnesses at a hearing shall be placed under oath.

ORDER OF PROCEEDINGS AT THE HEARING

A. After the oaths are administered, the Customer shall summarize his position of the dispute, stating briefly what relief he is seeking. The Businessman shall then present a summary of his position and relief sought.

B. The Customer shall next present his claim, evidence and witnesses, if any, and submit to questions from the Arbitrator. The Businessman shall then do likewise. Parties may cross-examine.

C. Following the presentation of evidence, each Party shall briefly summarize his position, relating his claims to the proofs and testimony presented.

D. The order of proceedings may vary at the discretion of the Arbitrator in order to assure that full opportunity is given each Party to present all evidence necessary for a decision.

E. The Arbitrator shall declare the hearings closed if no Party has further evidence to offer or witnesses to present.

ADMISSION OF EVIDENCE

The Arbitrator shall judge the relevancy of the evidence and may request additional evidence from either Party. He may refuse to admit evidence deemed irrelevant, stating reasons therefor.

ADDITIONAL PARTIES

In resolving any consumer dispute where someone other than the Businessman and Customer are necessary to resolve all issues, and where such person has agreed to the issues presented and to be bound by arbitration, the Arbitrator shall name him a Party to the dispute and have complete discretion to include such Party in the proceedings.

ADJOURNMENTS

The Arbitrator may adjourn the proceedings upon the request of a Party or his own motion.

METHOD OF DECISION

All matters of concern submitted to an arbitration panel shall be settled by a majority vote, including procedural questions and issues relating to the Award. The decision of the majority shall be deemed to be the decision of all members of the panel, and no dissenting opinion shall be issued.

REOPENING OF HEARING

At the discretion of the Arbitrator, a hearing may be reopened upon his motion or the motion of a Party. If a hearing is reopened, the time within which an Award must be made is measured from the closing of the last hearing. No hearing shall be reopened after an Award has been made except as provided by state law.

CONSERVATION OF PROPERTY

The Arbitrator may issue such orders as necessary to safeguard property which is the subject matter of arbitration or the position of the Parties.

SUBPOENA POWERS; DEPOSITIONS

The Arbitrator in Missouri and Illinois may compel the attendance of witnesses and the production of relevant documents according to procedures established by state law. The Arbitrator may authorize the taking of depositions of witnesses who are unable to attend the hearing.

AFFIDAVITS

Written affidavits if properly sworn to and notarized will be admissible in lieu of oral testimony, at the discretion of the Arbitrator, and if not objected to by the other Party.

WAIVER OF RULES

Any Party who proceeds after knowledge that a provision of these Rules has not been complied with and who fails to object thereto in writing prior to the time within which the Award is to be made shall be deemed to have waived his right to object.

EXTENSION OF TIME

The Parties may modify any period of time specified in these Rules by mutual agreement and the approval of the Arbitrator. The Arbitrator may extend any time period in these Rules except the period established for making an Award. The Administrator shall notify the Parties of any time extension.

THE AWARD

A. Time

The Arbitrator shall render a signed Award notarized if required by law, no later than ten days from the date on which the final hearing is closed. If additional materials are to be submitted beyond the final hearing date, the time for an Award shall be ten days from the receipt of such materials. If oral hearing is waived and the Arbitrator requires the submission of necessary written documents, the time for an Award shall be ten days from the receipt of such documents.

B. Scope

The Arbitrator may grant any relief or remedy within the scope of the Arbitration Agreement deemed just and equitable and allowable under state law.

C. Modification of Award

If there is a mistake of fact of miscalculation of figure on the face of the Award, the Administrator shall bring this to the attention of the Arbitrator, at whose discretion the appropriate modification will be effected. The Administrator shall transmit any such modifications to the Parties immediately upon receipt and posting.

D. Settlement

If the Parties settle the dispute prior to the rendering of the Award, the Administrator, upon written notice and verification of such settlement, shall terminate the proceedings and so notify the Arbitrator. Upon request of the Parties, the Arbitrator may, at his discretion, reduce any such settlement to a written Award.

E. Form and Filing

The Award shall be recorded on the Award Form and transmitted to the Administrator. The Administrator shall forward copies of the Award to the Parties and assist with filing the Award in the proper court where such is required under state law. Public disclosure of any Award may not be made unless all Parties agree in writing.

INTERPRETATION OF RULES

The Arbitrator shall interpret these Rules insofar as they relate to his powers and duties. Questions beyond the knowledge or expertise of the Arbitrator shall be referred by the Administrator to the Director, Consumer Arbitration, Council of Better Business Bureaus, Inc.

IN THE MATTER OF

KROGER COMPANY

Docket 9102. Interlocutory Order, June 14, 1978

Order denying respondent's application for review of ALJ's orders of October 18 and November 15, 1977.

ORDER DENYING APPLICATION FOR INTERLOCUTORY REVIEW

Respondent the Kroger Company has applied for review, under Rule Section 3.23(b), of the administrative law judge's orders of October 18 and November 15, 1977, which resulted in the striking of Kroger's Second Affirmative Defense from its Answer and denial of leave to amend that defense. Authorization to apply for review was granted by the administrative law judge's order of January 9, 1978.[1]

The defense at issue is the version of Kroger's Second Affirmative Defense set forth in its Motion for Leave to Amend Answer:

> ### *Second Affirmative Defense*
>
> The Complaint is an arbitrary and capricious exercise of the Commission's enforcement discretion and an abuse of that discretion. Respondent's Price Patrol advertising constituted responsible and good faith comparative price advertising. That advertising was based upon surveys of Respondent's and its competitors' prices. This followed the procedure directed by the Commission for supporting comparative price advertising. Other advertisers, including other retail food outlets, have made and are making more sweeping pricing claims with a less adequate or no basis therefor. The Commission is aware of the advertising of Respondent's competitors, having complained in public documents of the widespread use by retail food outlets of claims such as "lowest prices" and "discount prices." In these circumstances, the Commission's decision to proceed solely against Respondent, and not to proceed against other retail food outlets, will unlawfully preclude Respondent from forms of price advertising permitted to others and will place Respondent at a substantial disadvantage against its competitors. Furthermore, to proceed solely against Respondent violates the Commission's policy which requires that it take corrective action on an industry-wide basis where it perceives that several members of an industry are engaged in the same type of practice. Based upon the foregoing, the Complaint also deprives Respondent of equal protection of the laws in that the Commission is engaging in intentional and purposeful discrimination against Respondent in its enforcement of the Federal Trade Commission Act.

Commission review of interlocutory orders, including those applications for review authorized by the administrative law judge pursuant to Section 3.23(b) of the Commission's rules, is discretionary.[2] In exercising our discretion to entertain applications for interlocutory review, we have been guided largely by the criteria set forth in the rule for the law judge's determination. Because we disagree with the law judge that these criteria are satisfied here, we deny the application.

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[1] This is a vastly simplified history of the pleadings and rulings relating to the substantive issue of the striking of Kroger's Second Affirmative Defense, but it seems adequate to the task at hand. Had complaint counsel raised the question whether application for review was timely filed under Rule Section 3.23 (b), it would have been necessary to determine with more precision from which of the administrative law judge's several orders, including his ruling on the motion for reconsideration, appeal was sought. Under the circumstances, however, we will treat any necessary application for extension of such time as made and granted, and pass on to consideration of the application for review.

First, we find little if any ground for difference of opinion on the proposition that a respondent is not entitled to avoid litigation or liability by a showing that it has been "singled out" from among a number of possible wrongdoers. *FTC* v. *Universal-Rundle Corp.*, 387 U.S. 244 (1967); *Moog Indus., Inc.* v. *FTC*, 355 U.S. 411 (1958). Respondent contends that it has not violated Section 5 as alleged, but that, if it has, the Commission should not have sued only it at this time and should instead have proceeded on an "industry-wide basis," presumably either by suing respondent and all its competitors simultaneously, or by engaging in rulemaking. The decision whether to proceed against allegedly illegal practices by individual enforcement proceedings or by action of more general application is one within the broad discretion of the Commission. *Moog Indus., supra*, 355 U.S. at 413. See also, *e.g.*, *NLRB* v. *Bell Aerospace Co.*, 416 U.S. 267, 290-95 (1974); *Central Ark. Auction Sale, Inc.* v. *Bergland*, 570 F.2d 724, 727 (8th Cir. 1978).[3]

No court has held that the Commission has abused its discretion under the *Moog* standard, and we do not think it is likely that such a showing will be made with any frequency. It is not necessary here to try to define the specific circumstances in which we believe that a respondent might be entitled to relief under a theory of selective enforcement, as it is sufficient to observe that those set forth in respondent's second affirmative defense plainly are not.

Nor does the striking of the defense as respondent suggests, deny it any opportunity to proffer evidence on the subject of remedy at an appropriate time,[4] or to make arguments in this vein based on such evidence on the subject as the record may contain. Cf., *e.g.*, *Universal-Rundle Corp.*, 66 F.T.C. 1538 (1964) (evidence of competitive impact of order proffered and considered on motion to stay, withdraw and stay reentry of order); *C.E. Niehoff & Co.*, 51 F.T.C. 1114 1153 (1955) (assertion that order recommended by examiner would destroy respondent's business if competitors were not similarly restrained considered on appeal to Commission). Rather, deferral of the issues suggested by the second defense will tend to assure that, if necessary to address at all, they can be considered in a more relevant, focussed, and concrete context.[5]

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[2] Section 3.23(b) provides that:

> application for review of a ruling by the Administrative Law Judge may be allowed only upon request made to the Administrative Law Judge and a determination by the Administrative Law Judge in writing, with justification in support thereof, that the ruling involves a controlling question of law or policy as to which there is substantial ground for differences of opinion and that an immediate appeal from the ruling may materially advance the ultimate termination of the litigation or subsequent review will be an inadequate remedy. The Commission may thereupon, in its discretion, permit an appeal.

[3] The law judge's ruling is not in conflict with anything we said in denying a motion for reconsideration in *Ger-Ro-Mar, Inc.*, 84 F.T.C. 543 (1974), *aff'd as modified on other grounds*, 518 F.2d 33 (2d Cir. 1975), where we observed in passing that "a claim that the Commission has abused its discretion is *at best* an affirmative defense * * *." *Id.* at 546 (emphasis added). No question was there presented as to the proper procedure for raising such an issue, and the Commission held only that on the evidence profferred the respondent had failed to carry its burden of showing that the use of similar practices by its competitors meant that an order should not issue against it. In *J.J. Newberry Co.*, 80 F.T.C. 1016 (1972), the Commission reversed the law judge's grant of a respondent's request for discovery in aid of a selective enforcement defense, but specifically noted that the propriety or sufficiency of such defense was not presented or decided on the appeal. *Id.* at 1019 n.5.

The other criteria of Rule 3.23(b) likewise appear not to be satisfied. It is difficult to see how review of the law judge's decision at this stage of the proceeding will materially advance the ultimate termination of the litigation. Since the allegations of respondent's second affirmative defense, even if proved, are clearly not grounds for dismissal of the complaint, and since they may, in any event, be considered by the law judge or the Commission in determining the appropriate relief when and if a violation is found, holding the proceedings in abeyance to consider a question of pleading could accomplish only delay.

For similar reasons we are unable to conclude that respondent's appeal raises a "controlling question of law or policy" or that "subsequent review will be an inadequate remedy." Confined as they properly are to the question of remedy, the questions respondent raises in its second affirmative defense can hardly be said to be "controlling." Moreover, the adequacy and appropriateness of an order in light of the violations found is a proper question for appellate review under the applicable standard, even if the issue was not raised as an "affirmative defense." Thus, not only will subsequent review provide an adequate remedy, but it is the only appropriate context in which to consider respondent's contentions. Only after a full administrative hearing, and the actual delineation of an order, can any order be adequately assessed in the light of not only the record developed before the law judge, but also the probable impact of the order guaged in the context of competitive conditions, not as they exist at the time of the complaint, but as they exist or are likely to exist at the time of the order or thereafter.

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[4] In striking the defense, the law judge seems to have assumed that only such evidence and arguments as tended to show that respondent's business would be "destroyed" by the proposed relief would be appropriate for the Commission's consideration. While that standard reflects the very limited scope of a court's authority to set aside a Commission order as an abuse of discretion, other matters might well be considered, both by the law judge and the Commission, in the exercise of that discretion.

[5] Should the Commission find a violation and issue an order, the relevant inquiry under the general heading of selective enforcement would presumably focus on the scope and competitive impact of such an order. That inquiry might in turn require consideration of such questions as whether, where and to what extent the respondent or its significant competitors were then engaging in the practices found unlawful or proscribed by the order; whether the Commission had taken or was proposing to take action concerning such activities of the competitors; and whether by virtue of Section 5(m) of the FTC Act, 15 U.S.C. 5(m), the competitors would be facing sanctions comparable to those facing respondent for engaging in the activities in issue.

Accordingly, *it is ordered*, That respondent's application for review of the administrative law judge's orders of October 18 and November 15, 1977, is denied, for the reasons stated herein.

Commissioner Clanton voted in the negative, stating that he would have reached the same result but would have granted the application for review.

IN THE MATTER OF

G C SERVICES CORP., ET AL.

MODIFYING ORDER, IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL TRADE COMMISSION ACT

Docket C-2511. Decision, April 16, 1974 — Modifying Order, June 21, 1978.

This order reopens the proceeding and modifies the cease and desist order issued April 16, 1974, 39 FR 17100, 83 F.T.C. 1521, by substituting for Paragraph 6 of the original order, one that extends the time period postdated checks may be held from 15 days to 60 days, if specified requirements are satisfied before checks are deposited.

ORDER REOPENING PROCEEDING AND MODIFYING ORDER TO CEASE AND DESIST

By petition filed December 20, 1977, pursuant to Rule 3.72(b)(2), petitioner G C Services Corporation has requested the Commission to modify its order of April 16, 1974, to permit respondents to hold postdated checks for an unlimited period of time as long as certain requirements are met. The Director, Bureau of Consumer Protection, has filed an answer wherein he advises that he opposes the relief originally sought by petitioner but does not oppose alternate relief which would permit respondents to hold postdated checks for a maximum of sixty days as long as certain additional requirements are satisfied. The Director, Bureau of Consumer Protection, further advises in his answer that this alternative relief has been discussed with respondents and they do not object.

In support of their proposed modification respondents rely on the recent passage of Pub. Law 95-109, the "Fair Debt Collection Practices Act," 15 U.S.C. 1601, *et seq.* Section 808 of the Act (15 U.S.C. 1692f) prohibits a debt collector from using any "unfair or unconscionable" means to collect or attempt to collect any debt. Without limiting the general application of this, the Act continues to specify certain specific violations of the section. With regard to the use of postdated checks, the Act prohibits debt collectors from (1) accepting a check postdated by more than five days unless the alleged debtor is notified in writing of the debt collector's intent to deposit such check three to ten business days prior to deposit; (2) soliciting any postdated check for the purposes of threatening or instituting criminal prosecution; and (3) depositing or threatening to deposit any postdated instrument prior to the date on the instrument.

Respondents request that the Commission modify the order to permit GCSC to utilize postdated checks in a manner consistent with the Act. As an additional safeguard, GCSC would provide written notification of each of debtors' rights, pursuant to the Act, with regard to postdated checks as noted above.

The Bureau in its Answer to the Petition agrees that the proceeding should be reopened. The Answer submits that the order should be modified to permit alleged debtors and respondents greater flexibility in the use of postdated checks. However, the Bureau suggests an alternative modification to extend the period respondents could accept postdated checks from fifteen to sixty days with the additional safeguard that ten days prior to deposit respondents obtain or make good faith efforts to obtain permission from the alleged debtor to deposit the check. If they do not meet this requirement, they will be unable to deposit the check. Nothing in the order or modification shall limit respondents' obligations to otherwise fully comply with the requirements of the Fair Debt Collection Practices Act.

The Commission, having carefully considered the petition and answer thereto, has determined that the alternate relief as set forth in the answer be granted. The modification suggested by the Bureau would allow respondents greater flexibility to use postdated checks while insuring that alleged debtors are adequately protected. Respondents have alleged a legitimate benefit to consumers and competitive need for extending its ability to use postdated checks. However, respondents' proposed modification would obligate it to do little more than the Act already requires. The Commission is persuaded that extension of the time limit and the permission requirements for holding postdated checks would provide consumers and respondents with greater flexibility without unduly jeopardizing alleged debtor's rights.

Accordingly, *it is ordered*, That the proceeding be, and hereby is reopened for the limited purpose of modifying Paragraph Six of the Commission's order of April 16, 1974.

Further, *it is ordered*, That the order to cease and desist be, and hereby is modified by striking Paragraph Six and substituting therefor the following:

6. Receiving from alleged debtors postdated checks which will be held by respondents or their representatives for more than 60 days after receipt, *Provided* that, for any postdated check held for more than fifteen business days, no such postdated check shall be deposited unless respondents not more than ten nor less than three business days prior to such deposit (1) obtain permission to deposit such check from the alleged debtor or (2) make a good faith effort to contact and obtain permission from the alleged debtor. A "good faith effort" shall consist of three telephone calls to the alleged debtor's known telephone

contact, unless circumstances would make such efforts unreasonable. Failure to make contact would not relieve respondents of the obligation to notify in writing the alleged debtor of respondents' intent to deposit such check. Nothing in this order shall limit any duty of respondents to comply fully with the provisions of the Fair Debt Collection Practices Act, 15 U.S.C. 1692.

IN THE MATTER OF

FRUEHAUF CORP.

Docket 8972. Interlocutory Order, June 22, 1978

Order denying respondent's petitions to reopen and set aside Commission's divestiture order of February 22, 1978.

ORDER DENYING PETITIONS TO REOPEN AND SET ASIDE ORDER

By motions filed on May 10 and May 15, respondent Fruehauf has petitioned the Commission to reopen this proceeding and set aside the Commission's decision of February 22, 1978 which ordered divestiture by Fruehauf of the assets of the Kelsey-Hayes Company other than those unique to Kelsey-Hayes' Aerospace and RV Agricultural groups.

The asserted bases for Fruehauf's petition are several developments in the market for antiskid braking devices (ASBD). Fruehauf cites principally the decision of the Ninth Circuit in *Paccar, Inc.* v. *National Highway Traffic Safety Administration*, Nos. 75-1017, 2831, 3128 (April 17, 1978) ordering suspension of FMVSS 121 as it applies, *inter alia*, to truck trailers, because of defects in the procedure by which the standard was promulgated. Fruehauf also cites the initiation of a rulemaking proceeding by NHTSA to reconsider the standard, as well as introduction of bills in Congress to repeal the standard. All these developments, in Fruehauf's view, raise the possibility of changes in the ASBD market, and accordingly Fruehauf asks the Commission to withdraw its order, take further evidence and eventually reconsider its determination that divestiture is warranted. For the following reasons we believe that such a course of action is unwarranted and not in the public interest, and accordingly, we decline to reopen this proceeding.

The Commission found that violations of law had occurred in *three* markets—heavy duty wheels, truck trailers, and antiskid braking devices. Findings of violation in the first two of these markets are in no way altered or subject to potential alteration by the new information presented by respondent. With respect to the ASBD market, the Commission's finding that the merger was unlawful when it occurred is also not disturbed. To be sure, the information presented by Fruehauf does raise *a possibility* that at some unspecified future date the merger will no longer continue to threaten competitive harm with respect to the production of antiskid braking devices. This *might* occur, for example, if Fruehauf ceased permanently to purchase any substantial quantities of ASBD. Whether this *will* occur, however, or when, is highly problematical. The Ninth Circuit's decision (which at the present time has been stayed pending a decision by NHTSA as to whether to seek certiorari)[1] is without prejudice to the right of NHTSA to reimpose the same or similar requirements based on further hearings. Moreover, Fruehauf might remain a major purchaser of ASBD even were it under no legal obligation to use the device.

At the present time, therefore, the Commission has no basis upon which to alter any of the conclusions reached in its opinion.

It would clearly be unwise for the Commission to suspend proceedings in this matter indefinitely merely because of the possibility that further developments, whose date of occurrence cannot be forecast, might dissipate some of the effects of a merger we have concluded to be illegal.[2] This is especially true inasmuch as the violations found in heavy-duty wheels and the truck trailer markets are not in any way affected by the new developments. Assuming *arguendo* that the occurrences cited by respondent ultimately lead to elimination of the anticompetitive effects of the merger with regard to ASBD, the merger will still continue to exert anticompetitive effects in the heavy duty wheel and truck trailer markets. Since the market for heavy duty wheels is much larger than that for ASBD, and since Kelsey-Hayes' assets devoted to heavy duty wheels far exceed those devoted to ASBD,[3] it is clear that the lion's share of harm found to have occurred will persist under any circumstances.

The Commission ordered that Fruehauf divest Kelsey-Hayes except for assets unique to its Aerospace and R–V Agricultural Groups. This order was premised upon our view that total divestiture is ordinarily the remedy to be preferred in a merger case. While we were prepared to depart from this formulation to the limited extent of exempting assets clearly unrelated to the Automotive Products Group involved in the implicated markets, we concluded that attempting to carve out any lesser entity would be unwarranted by the record before us, which reflects only that Kelsey-Hayes has been a viable company, and not that those of its assets devoted to wheel production or ASBD production could be feasibly severed and made into viable units. Assuming *arguendo* that it were to transpire in several years that injury was no longer threatened in the ASBD market, our conclusion as to the appropriate remedy in this case would remain the same, because with respect to heavy duty wheels the record provides no basis on which to conclude that Kelsey-Hayes' market position could be transferred to another company which is not a competitor or a purchaser and which would be able to maintain Kelsey's position in the market.[4] For these reasons, the Commission concludes:

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[1] NHTSA has apparently determined to seek certiorari, and has also extended indefinitely the comment period in its rulemaking, which would appear to eliminate the possibility that it will imminently revoke the requirement of antiskid as to truck trailers *sua sponte*. 43 F.R. 24,871 (June 8, 1978)

[2] With regard to these "further developments," we must emphasize that they bear no relationship to the evolution of ASBD into a components market, urged upon us by respondent in its appeal from the initial decision. Our conclusions as to that remain undisturbed.

[3] As we noted in our decision, Kelsey's Gunite plant, at which wheels are made, accounted for $41 million in assets, vs. $3–7 million for the Brighton plant which makes ASBD. (fn. 35). Sales of ASBD in *1975* were around $41 million vs. *1972* heavy duty wheel sales of $240 million.

(1) The information presented by respondent provides no grounds to warrant disturbing our conclusion that this merger violates Section 7 with respect to three markets.

(2) The information presented offers no grounds to conclude at the present time that the continuing unlawful effects of the merger will in any way be dissipated.

(3) Even if the events discussed by respondent should at some future time lead to a dissipation of the continuing anticompetitive effects of the merger with respect to the ASBD market, this would not alter the Commission's conclusion that the divestiture order entered on February 22 is appropriate.

Therefore,

It is ordered, That respondent's petitions to reopen and set aside the Commission's order of February 22 be denied.

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[4] As we noted in fn. 36 of our opinion, it does remain open for Fruehauf to demonstrate affirmatively that the divestiture ordered by the Commission is not necessary. This it may do by presentation of a purchaser to the Commission which is not a manufacturer or purchaser of wheels or ASBD and which is capable of maintaining Kelsey-Hayes' market positions in those fields. Obviously, if Fruehauf were able to couple the production of a suitable purchaser for wheels with a showing that it was no longer a purchaser of ASBD, the Commission would give serious consideration to modification of its order. However, it is wholly speculative at this time as to whether Fruehauf could produce such a purchaser, and Fruehauf could surely not show at present that it has ceased permanently the purchase of ASBD. To delay indefinitely action to redress the effects of a merger found to be illegal, merely because future developments might possibly permit the law-violator to argue that a lesser remedy is sufficient, would be gross irresponsibility on the part of this agency.

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Proposal for financing promotional campaign to increase onion consumption in the U.S. by soliciting contributions from companies supplying material for or manufacturing onion containers, File 783 7003.

Opinion Letter

January 16, 1978

Dear Mr. Daniel:

This responds to your request, on behalf of the National Onion Association, for an advisory opinion concerning a proposed promotion plan.

It is the Commission's understanding that the Association would contact companies that supply materials for or manufacture onion containers ("container companies"). These companies would be asked to contribute one cent per container to the Association, which would use these funds to advertise and promote onion consumption. In anticipation of the one cent contribution being passed on to the purchasers of the containers, the proposal also provides that those growers who do not wish to participate in the program may obtain refunds from the Association after presenting proof of purchase from participating container companies.

The Commission, in prior advisory opinions, has recognized the inherent prospect for coercion where a trade association contacts suppliers in order to have the suppliers follow a proposed course of action. For example, when the National Association of Sporting Goods Wholesalers requested advice on a proposal to recommend procedures for prepaid freight to the manufacturers who sold goods to the Association's members, the Commission refused to approve the plan, stating:

> "Even if unaccompanied by any intent to force the manufacturers to adopt the policies set forth in the recommendation, there is implicit in such recommendation by the wholesalers too grave a danger that it will serve as a device whereby the concerted power of the members of the Association is brought to bear to coerce the manufacturers to conform their pricing policies to the restrictive standards of the recommendation, or at the very least as an invitation to enter into agreements among themselves to do so." (File No. 683 7106). [16 CFR 15.246, 73 F.T.C. 1333]

See, also, Printing Industries Association, Inc. of Southern California, File No. 683 7002 (Commission disapproved of plan to have Association discuss proposal for paper manufacturers to guarantee that a quoted price would remain firm for a definite time) [16 CFR 15.137, 72 F.T.C. 1042]; Automotive Wholesalers of Illinois, File No. 663 7036 (Commission disapproved of plan to adopt and transmit to suppliers recommendations concerning price changes and refund policies) [16 CFR 15.15, 69 F.T.C. 1203]. These opinions recognize the implied coercion where a trade association makes "suggestions" to the suppliers of its members.

Accordingly, after careful consideration, the Commission has concluded that it cannot give its approval to the promotion plan. While the Association has represented that nothing would happen to those container companies that did not participate in the program, the common interest of the Association's members in the program's success carries with it implications of potential concert of action. There is, implicit in the program, a grave danger that it could serve as a device whereby the concerted power of the members of the Association might be brought to bear to coerce container companies into participation in the program. Accordingly, the Commission is unable, under the laws it administers, to sanction the Association's program.

By direction of the Commission.

Third Supplemental Letter Relative to Request

May 9, 1977

Dear Mr. Sheehan:

This is to confirm our recent telephone conversation and answer the question that you posed during same.

Three different types of onion containers are in general use. These are a poly-vinyl mesh material which costs 28¢ a piece in Colorado, a paper mesh material which costs 31¢ a piece in Colorado, and the cartons which are used by some growers which cost growers 42¢ a piece in Colorado. The poly-vinyl mesh and the paper mesh hold 50 lbs of onions each. The cartons hold between 40–50 lbs of onions.

During our telephone conversation I also reiterated that some of the onion grower committee members of National Onion Association as well as myself would be happy to meet with you in Washington, D.C. to discuss our project if this would be useful to you.

I also inquired of you if it would be helpful if the Department of Agriculture discussed this matter with you and let you know what their position was with regard to same. As to this latter point, you advised me that you would be back in contact with me and advise as appropriate.

Your assistance is appreciated.

Yours truly,
/s/ Jerry C. Daniel

Second Supplemental Letter Relative to Request

April 20, 1977

Dear Mr. Sheehan:

This letter is in written response to your telephone request of Monday, April 18, 1977.

You asked that I advise you how National Onion Association intends to approach container suppliers and manufacturing companies and furnish you with a sample of any letter agreement we are contemplating using.

A rough draft only has been prepared of the type of letter that we are contemplating using.* It is not complete and before it is complete, will need to have language in it to the effect that onion producers can write to the National Onion Association and obtain a refund on any monies that the container manufacturer or supplier passed on to them when the producer purchased onion containers from these entities. This is a rough draft that was made up very early in these considerations and undoubtedly can be improved and made more accurate. Committee members on the promotion committee of the National Onion Association have already been putting out feelers by telephone, personal contact and letter with container suppliers and manufacturers to ascertain if they have any interest at all in going along with the plan that is being developed. Results are very sketchy at this point in time and many of these companies want to know what the FTC position is on our request for an advisory opinion before committing themselves. Of course, we are not asking for any firm commitments at this time.

You asked me what would happen if a container supplier or manufacturer did not care to participate in the program. As far as NOA is concerned, nothing would happen. They would just not be part of the program and we would hope that enough companies are part of the program that sufficient monies will be raised to do some good.

In checking with individuals on the promotion committee, they feel that there is no question but that the staff can handle any refund program and all that would be necessary for a grower to obtain a refund is to show proof of purchase subsequent to the date that the container supplier or manufacturer agreed to go along with the promotion plan of NOA.

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* The draft letter is not reproduced herein.

There appears to be no information on how many individual onion growers are producing onions in the seventeen state area mentioned in my prior letter or how much tonage these onion growers are producing on an individual basis. This is not public information and apparently the statistics are not being gathered by any organization.

Again I would reiterate that I and members of the committee of the National Onion Association would be happy to come to Washington, D.C. to meet with you and fully explain the concept that we are hoping to evolve.

Thank you for your assistance in this matter.

Yours truly,

/s/ Jerry C. Daniel

First Supplemental Letter Relative to Request

April 13, 1977

Dear Mr. Sheehan:

This is in reply to your telephone request of Monday, April 11, 1977.

The information that I am furnishing you is the best that can be developed by the National Onion Association at this time, but we feel is relatively accurate.

There are seventeen states which are onion producers of both the storage and non-storage onions. Some other states grow small quantities of onions but do not ship them out of state and are not counted in our tabulation.

Of the seventeen states growing storage and non-storage onions, there are 93,962 planted acres. Of these, 38,834 acres are actually planted by NOA members – or 41%. The amount of onions handled by NOA members, however, is 72.4%.

NOA data does not show how many growers of onions there are in the United States and we do not believe it is possible to determine this number with any accuracy.

The areas that have marketing orders and the purpose of the orders are as follows:

Idaho – East Oregon – Promotion of specific onion and research.
Michigan – Research
New York – Research
Texas – Quality control

National Onion Association cannot go to onion growers directly to raise funds for promotion and advertising purposes because of the logistics impossibility. NOA has neither the manpower nor the money to effect a campaign which would contact the growers, advise them of the plans and benefits and arrange the documents that would be necessary to implement such a program. In the approximate 1959–60 onion growing season, a voluntary plan of this type was attempted by the National Onion Association but failed miserably. Again, the logistics problems could not be overcome. Obviously in this type of a plan there is a need for a consistent, even flow of funds that can be relied on and the above considerations are what led to the development of the plan that we are asking an advisory opinion on from the FTC.

Thank you so much for your assistance and cooperation. If there are any questions that we can answer, please let us know. We also hope that a few of us will be able to visit you in Washington, D.C. to fully explain the concept before you.

Yours truly,

/s/ Jerry C. Daniel

Letter of Request

March 7, 1977

Dear Mr. Secretary:

The National Onion Association is starting to evolve a plan which is hoped will be effective in increasing the use and consumption of fresh onions particularly in the United States. The purpose of this letter is to ascertain from your commission if your attorneys feel that the plan of the National Onion Association steps over the line between what is permitted and what is considered as illegal under various anti-trust and other pertinent laws. The National Onion Association has proposed the following plan but it is not currently being followed.

The National Onion Association is a non-profit Colorado corporation. It is a rather loose knit organization and therefore, does not have a great deal of cohesiveness or power as such pertains to control of members within the association, but does represent 50–75% of the production of onions in the United States.

The leadership of the association has determined that it would be to the benefit of onion farmers, the association itself and manufactors and distributors of onion containers if the consumption of onions could be increased in the United States through a promotion and advertising campaign. As a corollary to this, you might be interested in knowing that consumption of onions in the United States is far below that of most foreign countries. Since the association does not have a Federal or State marketing order and is not a cooperative and does not have viable means of raising much money, the following plan is being considered to pay for a vast advertising campaign.

The association wants to approach the container manufactors and suppliers who furnish onion containers and have them furnish to the association, an amount equal to one cent for each container that they manufacture or supply.

There are two major suppliers of raw materials for onion containers and there appear to be approximately sixty manufactors of onion containers.

The association estimates that the proposed plan would raise about one half million dollars per year for use in advertising the various attributes of onions. Since the association is a non-profit organization, it would use all monies for the advertising and would not profit from the venture itself. Of course, all members of the association, as well as consumers, hopefully would benefit from the proposed plan.

It is understood that the container companies would not have to pass on the one cent per container increase to its onion producers, but as a practical matter, probably would do so. Since the association does not comprise all onion producers in its membership, it is planned that any individual, member of the association or not, who desired to not participate in the plan could write to the association, show proof of the purchase he made and receive back the penny per container that would be attributable to him.

Although it would be an administrative nightmare and the association leadership does not feel it would be fair for non-members to benefit and hang on to the coattails of members' actions and expenditures, it is theoretically possible to limit the program to members of N.O.A. who purchase containers from container suppliers and companies.

Under the proposed plan, the association would act in effect, as an advertising agency and would take such actions as appear reasonable to improve the image of the onion and to promote an increase in the consumption of onions. It would use all of the funds raised in this manner for this purpose.

It would be very much appreciated if the legal department or whoever you feel is appropriate in the FTC would contact me and advise if there is any prohibition on the plan being considered by the association. If there are any limitations or any areas that you would want to caution us in, the information would be very much appreciated.

The association is anxious to implement the proposed plan in the immediate future and your prompt attention to this would be very much appreciated.

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Thank you for your consideration and attention to this matter.

Yours truly,

/s/ Jerry C. Daniel

"Jackpot" promotion for use in food retailing industry, involving a numbers matching protocol, is within Trade Regulation Rule for Games of Chance in the Food Retailing and Gasoline Industries, 16 CFR 419.

Opinion Letter

January 27, 1978

Dear Mr. Radcliffe:

This is in response to your request for advice concerning a "jackpot" promotion for use in the food retailing industry, involving a numbers matching protocol. Your inquiry is whether this promotion is a "game of chance" within the Commission's Trade Regulation Rule for Games of Chance in the Food Retailing and Gasoline Industries, 16 CFR 419.

As the Commission understands the promotion you propose, game pieces will be made available to potential contestants through outlets of a sponsoring food retailer (no purchase required). The game pieces will consist of small cards imprinted with twenty-five different, randomly placed numbers from the series of "1" to "25". Such numbers are not immediately visible, but are hidden beneath twenty-five opaquely surfaced panels. The number that may be disclosed by scraping away the surface of any such panel, therefore, is a matter solely of chance.

The game sponsor or user will have identified nine particular numbers from the "1" to "25" series, for each run of the game. Contestants are required to prepare their cards, or game pieces, by scraping away and uncovering nine only out of the twenty-five panels, thus revealing nine of the card's numbers. Contestants must turn in game pieces, so prepared, by closing time the last day of a contest month in order to be eligible. Two jack-pots are provided, one for $40,000 and a lesser one for $20,000.

A contestant having entered a game card matching eight of the nine designated winning numbers will win either the principal jack-pot of $40,000, or that jack-pot will be divided equally among all contestants who submitted game cards so qualifying. The $20,000 jack-pot will be awarded to contestants whose game cards match seven of the nine numbers designated. The reported odds of hitting eight out of the nine designated numbers is 1 in 14,190. The reported odds of hitting seven out of the nine, is 1 in 473.

The Commission concludes that the promotion is within the Rule. It is, first of all, clearly a "game of chance" as that term is used and understood in ordinary usage. It involves calculable odds of which consumers, under the Rule, should be apprised. It has no elements of a contest of skill. It does not appear to consist of a "one-shot" sweepstakes. Rather, it is a game at least susceptible of protraction over an extended period, during which contestants may be expected to return successively to a participating retail outlet for additional game pieces, in the hopes of winning.

The Commission has determined, accordingly, that the promotion should be conducted in conformity with each of the Rule's applicable provisions. Particular provisions of the Rule which, by their nature, clearly contemplate only games that involve pre-selected winning game pieces, are not applicable to your game and, therefore, you may properly disregard them. An example would be the second requirement of Section (b)(1), requiring disclosure (after a game has extended beyond 30 days) of the number of unredeemed prizes still available and the then existing odds.

The Commission's staff will remain available to provide any assistance you may need, if you find difficulty in determining which provisions of the Rule are properly applicable to your game.

By direction of the Commission.

Letter of Request

February 2, 1977

Dear Mr. Garvey:

As a producer of games and promotions for the super market industry, we at Radcliffe Advertising, Inc. have created a new type promotion which is similar to a game, but totally different in many ways. Because this is true, we would like to get an advisory opinion on this promotional technique. We think it is a sweepstakes or similar to a drawing, not a game.

The promotion works this way:

We give every contestant a sweepstakes card free. On the card are twenty-five numbers. . . .from one to twenty-five. Every card has all twenty-five numbers. . . .but arranged in a randomly different order on each card. These numbers are covered with an easily scratched off material. The customer is invited to remove any nine of the covered numbers, and told to match a given nine numbers. For example, match the numbers 1, 11, 21, 3, 13, 23, 5, 15, and 25. If she matches any eight of the nine numbers, she wins or shares a monthly jackpot of approximately $40,000. If only one person matches eight numbers (on one card), that person wins the entire $40,000. If more than one person matches eight numbers, the jackpot is divided equally among all those contestants.

In addition to this Giant Jackpot, there is also a Junior Jackpot of approximately $20,000. Any contestant matching seven of these numbers out of nine, wins or shares the Junior Jackpot in the same manner.

This is how the promotion works. We feel it is totally different from a game in the following ways:

1. There are no key cards. Every sweepstakes card has the same twenty-five numbers. Every and/or any card can win. . . .it is not necessary to get a key card to win.
2. Until the end of the month, we do not know how many contestants will participate in the jackpot, so therefore we cannot know how much each contestant will win. . . .only that each winning contestant will share a jackpot of a predetermined amount.
3. There is no mixing necessary of the sweepstakes cards because the arrangement of the twenty-five numbers on every card is different. There are no two cards alike in the entire promotion.
4. There is no possibility of adding additional winners to the sweepstakes because the jackpots are predetermined and we intend to give out all the money in the jackpots. In the event no one picks the number correctly, the jackpots are carried over and added to the next month's jackpot ad infinitum until the jackpots are given away.
5. The size of the prize depends solely on the number of contestants who guess correctly where the winning numbers are on the card.
6. The odds of determining the size of the prizes are not under our control but are strictly based on the luck of the contestants.

Several years ago, we submitted another promotion using this same jackpot idea to the commission for an opinion. The opinion of the staff was that this promotion, entitled "Jackpot Football", did not come under the game rule. We feel that this promotion is similar in nature and would not fall under the game rule.

In the running of this promotion, there is not a way we can fail to give out all of the jackpots. There is not a way we cannot properly mix the cards because the contestants in effect mix the cards with their choice of panels to uncover. There is no way we can control the size of prizes in any way because this is determined strictly by the luck of the contestants who submit entries.

We would appreciate an opinion of the staff of the Federal Trade Commission.

Sincerely,

/s/ Harry Radcliffe

1167

Compliance opinion as to whether a furniture manufacturer's proposed plan to grant special price quotations, under certain conditions, to dealers competing in bid situations would violate the order issued on June 30, 1967 (71 F.T.C. 1579), Dkt. C-1248.

Opinion Letter

January 31, 1978

Dear Mr. Moran:

The Commission has considered the request which is contained in your letter of April 27, 1977, as supplemented by letter of August 5, 1977, wherein you seek the Commission's advice pursuant to Section 3.61(d) of the Commission's Rules. This advice is sought to determine whether a proposed course of conduct whereby Herman Miller would grant special price quotations, under certain conditions, to dealers competing in bid situations, would be violative of the Commission's order issued on June 30, 1967, in the captioned matter.

The proposed plan would grant special price quotations to dealers in bid situations only. In order to receive the special price in a specific situation, a dealer would have to certify that it will submit a bid on that specific job. In addition, in order to obtain special pricing a dealer will have to agree that on the specific job he will not bid products competitive to those products for which he will obtain special price quotations from Herman Miller. This special pricing will be available to all dealers who carry the Herman Miller line, provided that the above conditions are satisfied, and all dealers will be so notified.

The above outlined plan is to operate in the context of bid solicitation by institutions. When an institution solicits bids for furniture, it may do so by specifying items by brand name (*e.g.*, 30 Herman Miller desk chairs), or by descriptive specifications (*i.e.*, by specifying size, color, finish, etc., for each item). Such a bid solicitation may involve a large number of different items, and, when brand names are specified, different items may call for different brands. It is the Commission's understanding that, under the proposed plan, when bids are solicited by specifying brands, and different items call for different brands, a dealer handling multiple lines who plans to quote the Herman Miller items and the non-Herman Miller items will receive special pricing from Herman Miller. It is also the Commission's understanding that when bids are solicited by descriptive specifications rather than by brand name, a multiple line dealer who wishes to bid Herman Miller products for some items and competing brands for other items will be precluded by the proposed plan from receiving

Herman Miller's special pricing on the items he wishes to bid Herman Miller.

It is the Commission's opinion, based on the facts submitted, that the proposed plan, if implemented, may raise questions under Section 5 of the Federal Trade Commission Act, and under the order issued in the above-captioned proceeding. If there are dealers who wish to quote Herman Miller products on some items and competing brands on other items, they will not be able to do so and still receive Herman Miller's special price. In effect, the Herman Miller special price might not actually be available to all dealers who wish to take advantage of it, and this would constitute a discrimination against those dealers.

By direction of the Commission.

Supplemental Letter Relative to Request

August 5, 1977

Dear Mr. Rossi:

Please excuse my delay in responding to your inquiry of May 20, 1977, in the above referenced matter. A combination of conflicting business trips and vacation schedules has prevented me from conferring with the necessary Company personnel to obtain the answers to your questions until now.

The following numbered paragraphs contain answers corresponding to the numbers of the questions posed in your May 20, 1977, letter.

(1) If Herman Miller were the named brand, it would be impossible for the dealer to bid a competing line along with Herman Miller in many cases because the manufacturer of the competing line would not give special pricing to the dealer if that manufacturer were aware that the dealer would be bidding Herman Miller. Moreover, even if a dealer had the ability to bid two competing lines, and an institution specifies "Brand X or equivalent," it would be a rare case when any particular dealer would bid more than one brand. Usually these specifications are the result of considerable pre-bid sales activity by dealers (sometimes in active participation with the manufacturer) and the dealers generally identify themselves with a specific brand during this pre-bid activity. Even if a dealer was not involved in the pre-bid sales effort with respect to a particular customer, that dealer is unlikely to bid the specified brand because he knows that some other dealer has established a preference with the customer on that product line through the pre-bid sales effort.

At this point two observations are in order. First, virtually every bid situation will attract a bid from each manufacturer either through a dealer for that manufacturer's product line or via a direct bid from the manufacturer. Consequently, a refusal by any manufacturer to quote a special price to any particular dealer will not prevent the customer from obtaining a competitive price on that product line. Second, it should be noted that all dealers are not dual dealers on competitive products, and in many cases a single-line dealer or dealers will be bidding against one or more dual-line dealers. This fact causes the following problem for the Company. Assume that Dealer A is a dual dealer for Brand X and Herman Miller, and that Dealer A has succeeded in convincing an institutional purchaser to specify "Brand X or equivalent" in its bid invitation. Dealer B is a Herman Miller dealer and a single-line dealer. If Herman Miller decides to have its product bid under these circumstances, it is faced with the prospect of either: (a) extending special pricing to Dealer B to enable the dealer to bid, in which case, under its present policy, the Company would also extend the special pricing to Dealer A (the dual dealer) which has already identified itself with a competitive product (Brand X) on that bid; or (b) extending no special pricing to any dealer and bidding the project direct to the customer. This is obviously a difficult position for the Company because disclosing its bid price to Dealer A is in effect disclosure to its competition, while bidding direct jeopardizes its relations with Dealer B.

(2) The answer to this question is substantially the same as the answer to the preceding question. Whether the purchaser's request for bids identifies the product by name or by description has no material affect on the responses of the bidders.

(3) Yes.

(4) Yes.

(5) Undoubtedly there have been occasions when a dealer has mixed product lines in a bid to a nonproprietary specification, but those occasions are rare. Generally, the dealer will bid one manufacturer's line rather than mix products in the bid.

(6) In the case posed under question (4), the dealer would not be precluded from obtaining special pricing under the proposed plan. However, if it is assumed that the case posed under question (5) would occur, then in that case the dealer would be precluded from obtaining the special pricing.

We trust that the foregoing is responsive to your inquiry. However, should you require additional information please feel free to contact us either by letter or collect telephone call at your convenience.

In closing, we would like to point out that while all competitors in the office furniture industry vigorously extol the virtues of their respective product lines as opposed to those of other manufacturers, these products are for the most part functionally equivalent in the antitrust sense. The proposed plan would have no adverse impact on interbrand competition; rather, the proposed plan would enhance the integrity of the interbrand competitive bidding process. Moreover, the proposed plan would have no significant adverse impact on intrabrand competition because the special pricing would not be denied to any dealer who had a genuine interest in bidding the Company's products. Accordingly, we believe that the proposed plan is consistent with the Commission's outstanding Order and antitrust laws generally. *Cf. Continental TV Inc* v *GTE Sylvania, Inc* [Current Materials Binder] Trade Reg Rptr ¶61,488 (U.S. Sup. Ct. 1977).

Thank you for your consideration.

Yours very truly,
VARNUM, RIDDERING, WIERENGO & CHRISTENSON

/s/ J. Terry Moran

Letter of Request

April 27, 1977

Dear Mr. Tobin:

In accordance with the Commission's rules, we are writing on behalf of our client, Herman Miller, Inc., to request advice on the question of whether the following described proposed course of action will constitute compliance with the Commission's order entered with the Respondent's consent on June 30, 1967, effective December 1, 1967 in the above referenced matter.

That order provides with respect to the offer and sale of furniture products that the Respondent shall cease and desist *inter alia* from:

> Discriminating, directly or indirectly, in the price of such products of like grade and quality by selling such products to any purchasers at net prices higher than the net prices charged to any other purchaser who in fact competes in the resale or distribution of such products with the purchaser paying the higher price.
>
> * * * * * * *
>
> Notifying, or otherwise communicating to, its customers, directly or indirectly that one or more of its customers will be favored in terms of price or otherwise, with respect to bargaining with, or submitting bids or otherwise quoting prices to, particular consumers or users of such products.

Herman Miller has continued to manufacture furniture products principally for office and institutional use since the date of that order. The Company's products are distributed mainly through independent dealers who purchase products from the Company and resell those products to office and institutional users with some occasional sales for residential use. Currently the Company has approximately two hundred authorized dealers for its products throughout the United States.

The office furniture market on a national basis encompasses an estimated $1,450,000,000 in annual sales. There are an estimated two hundred fifty manufacturers making sales in this market principally through independent dealers. Herman Miller dealers are not exclusive dealers. Most of them handle one or more product lines competitive to Herman Miller products. In metropolitan marketing areas, the Company will typically have more than one dealer.

Herman Miller is an industry leader in terms of innovation and design. An example of the Company's leadership is its Action Office ® product which pioneered the popular open-space office systems concept. Many competing manufacturers now market open plan systems. In recent times, the market for these products has become more price sensitive and purchasing of major quantities of these products systems by large institutions has become more bid-oriented.

These large institutional sales involve substantial design, specification and sales efforts by dealers prior to the bid process. Generally a dealer will pursue these prebid activities on behalf of one manufacturer's product line to the exclusion of other lines; in fact, the dealer may be competing for the "specification" against other dealers who are promoting a competing line of product. Frequently, when the specification is let for bid, it will encourage or permit bids for a named product line "or equal". Such specifications call for product quantities, product mixes and differing finishes and fabrics so as to preclude sales out of dealers' inventories, and dealers request special pricing and delivery quotations from manufacturers for the particular job. Manufacturers normally respond by pricing these jobs at an aggregate price lower than the sum of its regular prices for the variety of products which comprise the specification. (This is referred to as "special" pricing.) A manufacturer's pricing is predicated in large part upon its judgment of what price level it anticipates will be offered by competing manufacturers. Accordingly, price competition on such bids basically is price competition between competing manufacturers, since the product cost to the dealer has an overwhelming influence on his bid price.

In bid situations, Herman Miller makes its special prices available to all its dealers who are competing for such bids. Pursuit of this policy in some instances has placed the Company at a competitive disadvantage. In certain cases during the pre-bid process, a dealer who is a dealer both for Herman Miller and a competitive manufacturer may promote the competitor's product line and succeed in obtaining the specification of that line. That dealer will then bid only the specified line. That dealer, however, will also request Herman Miller's special pricing for the same job as an "equal". Making Herman Miller prices available to that dealer in advance of the bid submission is tantamount to disclosing Herman Miller's prices in advance to a competing manufacturer. That dealer is able to inform Herman Miller's competitor of the exact price Herman Miller is quoting for that bid, and the bidding process if subverted to the detriment of Herman Miller and the dealer or dealers who are promoting Herman Miller's products. On the other hand, in a reverse situation where a dual dealer obtains a Herman Miller specification, the competitive manufacturer will refuse to quote special prices to Herman Miller dealers who intend to bid the Herman Miller product.

Herman Miller desires to follow a policy equivalent to that of its competitors. Herman Miller proposes to notify its dealers that special pricing for specific bids will be granted to each dealer competing for such bid upon the condition that the dealer certify in advance:

(a) That he will submit a bid on that specific job; and

(b) That on that specific job he will not bid products competitive to those products for which he will obtain special price quotations from Herman Miller.

As a result of this proposal, combined with existing practices by other manufacturers, a dealer with multiple product lines will decide in advance which manufacturer he will represent on that specific bid, and will receive special pricing from that manufacturer only.

It is our view that pursuit of such a policy by the Company, as well as other manufacturers, would not be a violation of the Robinson-Patman Act, nor would it constitute a violation of the aforementioned provisions of the Commission's Order. Special pricing will be offered to all Herman Miller dealers on the same terms and conditions, subject only to the dealer's election to take advantage of the offer. On this basis, the Company would not be "discriminating" against nor "favoring" any particular dealer within the meaning of the Commission's Order. We believe that this conclusion is supported by the fact that the proposed course of action does not involve any aspect of the challenged conduct which resulted in the entry of the Commission's Order in 1967, and, further, by the fact that such an interpretation of the Order would be consistent with prior determinations of the Commission and the courts holding that discounts for prompt payment and quantity discounts do not involve "discrimination" where functionally available to all customers.

We respectfully request the Commission's advice as to whether the proposed course of action outlined above will, if pursued by the Company, constitute compliance with the Commission's outstanding Order. In the event the Commission's staff desires additional information or clarification of the proposed course of action, we will be happy to supply such information or consultation as the staff deems necessary. Thank you for your consideration.

Yours very truly,
VARNUM, RIDDERING, WIERENGO & CHRISTENSON

/s/ J. Terry Moran

Use of the name of the foreign manufacturer on the label of an imported covered product is permissible under the Textile and Wool Acts and their supporting regulations, File 783 7004.

Opinion Letter

February 6, 1978

Dear Mr. Boyett:

This responds to your request for advice concerning name identification requirements relative to imported goods of Sec. 4(b)(3) of the Textile Fiber Products Identification Act and Sec. 4(a)(2)(C) of the Wool Products Labeling Act. You have inquired in this regard whether the foreign manufacturer's name on labels and hangtags in lieu of the name or tradename (where applicable) or registered identification number of the American importer or distributor, is considered sufficient name identification under these Acts.

It is the Commission's interpretation of both Acts, and their supporting Rules, that the labels of covered products imported into this country may carry the name of the foreign manufacturer *or* the name or tradename (where applicable) or registered identification number of a person or firm marketing the product in the United States. An election to use the name of the foreign manufacturer, accordingly, is completely permissible. The foreign manufacturer's name, if used, must be that under which the firm does business. Responsibility for any misbranding of products under these Acts, however, rests with the person or firm introducing the product into commerce in the United States.

By direction of the Commission

Letter of Request

July 6, 1977

Dear Mr. Thomas:

In enforcing the provisions of the Textile Fiber Products Identification Act and the Wool Products Labeling Act on imported merchandise, we have noted numerous instances of the use of the foreign manufacturer's name on labels and hangtags in lieu of the name or tradename (where applicable) or registered identification number of the American importer or distributor. We would appreciate an advisory opinion as to whether the name of a foreign manufacturer would be considered sufficient name identification to comply with the requirements of Sec. 4(b)(3) of the Textile Fiber Products Identification Act and Sec.

4(a)(2)(C) of the Wool Products Labeling Act.

Sincerely yours,

/s/ Fred R. Boyett
Regional Commissioner of Customs

Opinion Letter

February 6, 1978

Dear Mr. Weiser:

It is the Commission's understanding that in lieu of appeal to the Commission for discretionary release of documents (your letter of May 3, 1977) you wish instead definitive Commission advice respecting the specified subject matter thereof, *viz.*, whether the name of the foreign manufacturer of an imported textile fiber product would be deemed to comply with Rules 16(a)(2) and 19(a) of the Rules and Regulations under the Textile Fiber Products Identification Act, as amended.

The Commission also has before it, at this time, a virtually identical request concerning the Textile Fiber Products Identification Act and, in addition, the Wool Products Labeling Act.

It is the Commission's interpretation of both Acts, and their supporting Rules, that the labels of covered products imported into this country may carry the name of the foreign manufacturer *or* the name or tradename (where applicable) or registered identification number of a person or firm marketing the product in the United States. An election to use the name of the foreign manufacturer, accordingly, is completely permissible. The foreign manufacturer's name, if used, must be that under which the firm does business. Responsibility for any misbranding of products under these Acts, however, rests with the person or firm introducing the product into commerce in the United States.

By direction of the Commission.

Supplemental Letter of Request

May 3, 1977

Sir:

In our initial request of March 18, 1977 (copy enclosed herewith), we asked for "all rulings, memoranda, opinions, and all other documents, published or unpublished, whereby the Federal Trade Commission's position with regard to whether the setting forth of the name of the foreign manufacturer of an imported textile fiber product would be deemed to comply with Rules 16(a)(2) and 19(a) of the Rules and

Regulations under the Textile Fiber Products Identification Act, as amended, is stated." The Commission responded by its letter of April 18, 1977 (copy enclosed) and stated that our request had been partially granted and those documents which were being withheld had been deemed to be exempt from mandatory disclosure as they were inter-agency or intra-agency memoranda or letters. As to the portion of our request which was granted, the Commission enclosed a multitude of documents which, we would assume, was responsive to our initial request.

We have now completed our review of the documents which the Commission forwarded to us and have determined that not a single one of them is at all responsive to our request of March 18th. Our request was simple and specific: we had asked whether a *foreign* manufacturer's name could be used on labels of textile products pursuant to the Textile Fiber Products Identification Act and specific regulations above cited. Not one of the advisory opinions forwarded to us had anything to do with that request (copies of all documents returned herewith).

Therefore, we are returning unpaid your bill of April 18, 1977 in the amount of $31.10 with our comment that unfortunately a lot of time-consuming and useless work has apparently been done by a Government employee who did not have the appropriate guidance in gathering the requested information.

Furthermore, it is requested that, as to the documents which were believed to be exempt from mandatory disclosure, the Commission exercise its discretion and release the material notwithstanding its allegedly exempt status. The reason we are requesting the release of this subject matter is that our client, Frederick Atkins, Inc., an importer of wearing apparel, desires to use the name of the foreign manufacturer on a particular label of wearing apparel in lieu of an RN number.

We would appreciate your earliest advice with regard to this appeal.

Very truly yours,
SIEGEL, MANDELL & DAVIDSON

/s/ Steven S. Weiser

1174

Responding Letter to First Request

April 18, 1977

Dear Mr. Weiser:

This is in further response to your letter dated March 18, 1977, concerning the above-captioned matter.

Your request is hereby partially granted, and copies of the documents are enclosed. Portions being withheld are deemed to be exempt from mandatory disclosure pursuant to 5 U.S.C. 552(b)(5) inter-agency or intra-agency memorandums or letters which would not be available by law to a party other than an agency in litigation with the agency.

You may petition the Commission within thirty (30) days for access to the material which is being withheld. You may petition either because you believe that the material is not exempt under the law, or because you believe the Commission should exercise its discretion and release the material notwithstanding its exempt status. If requesting discretionary release, you should state your interest in the subject matter and the purpose for which it would be used if access were granted. The request should be addressed to Freedom of Information Act Appeal, Office of the General Counsel, Federal Trade Commission, Sixth Street and Pennsylvania Avenue, N.W., Washington, D.C. 20580.

Please include a copy of your original request and this response by the Secretary with your appeal.

The first portion of your request, concerning the position taken by the Commission in the instant matter, is answered in the enclosed advisory opinions. Regarding the Commission's present posture, I suggest that you submit a request for an Advisory Opinion. I am enclosing a copy of Part 1, Subpart A – Industry Guidelines of the Commission's Rules of Practice, which describes the procedure for requesting an Advisory Opinion.

The duplication fees incurred in the processing of your request amounted to $31.10. Please remit this amount, payable to the Treasury of the United States, to Mr. Glenn Goodnight, Supervisor, Public Reference Branch, Room 130, Federal Trade Commission, Sixth Street and Pennsylvania Avenue, N.W., Washington, D.C. 20580.

The undersigned is deemed the sole official responsible for the denial contained herein.

Sincerely,

Letter of Request

March 18, 1977

Re: Freedom of Information Act
Request
Textile Fiber Products
Identification Act

Gentlemen:

Pursuant to the Freedom of Information Act (5 USC §552), request is hereby made for all rulings, memoranda, opinions, and all other documents, published or unpublished, whereby the Federal Trade Commission's position with regard to whether the setting forth of the name of the foreign manufacturer of an imported textile fiber product would be deemed to comply with Rules 16(a)(2) and 19(a) of the Rules and Regulations under the Textile Fiber Products Identification Act, as amended, is stated.

In addition to the foregoing, it is requested that you kindly advise us as to what is your present posture with regard to this question.

Very truly yours,

SIEGEL, MANDELL & DAVIDSON

Steven S. Weiser

1179

Proposed "raw material reporting system"—a statistical reporting program to be undertaken by an association of independent wire drawing companies, File 783 7005.

Opinion Letter

February 9, 1978

Dear Mr. Wasserman:

This letter is in response to your request for an advisory opinion concerning a proposed "raw material reporting system"—a statistical reporting program—to be undertaken by the Independent Wire Producers Association ("IWPA"), an association of independent wire drawing companies. Your request, in this connection, for confidential treatment is denied.

It is the Commission's understanding that under the proposed "raw material reporting system" each participating IWPA member would report on a regular basis to the statistical branch of the IWPA's management firm or to an independent economic analysis firm the following details of each applicable raw materials offer the member receives: the quantity, type, weight, foreign country of origin and price of carbon steel wire rod offered, the date the offer was received and the date terminated, and the calendar quarter of offered shipment.

The name of the foreign offeror and acceptance or rejection of the offer would not be reported. The IWPA's management firm or the economic analysis firm would collate the collected information and issue aggregate figures on a monthly basis to all participating members. The aggregate information would reveal neither the names of the reporting member companies, the specific prices offered, nor the names of the foreign offerors.

The Commission would not initiate proceedings against the IWPA if such a program were adopted provided that (1) the reported data is collected by a firm independent of the IWPA and its members, (2) no individual member's data is disclosed to any other member, and (3) none of the disseminated aggregate data reveal, directly or indirectly, the identity of foreign wire rod suppliers. You are cautioned, in particular, that the program must not be used in such a manner that it leads to a boycott, to the blacklisting of certain suppliers or groups of suppliers, or to any other unlawful trade restraint.

In its consideration of this matter the Commission does not wish to be understood as approving or agreeing with any economic or competitive aspect of the subject proposal unrelated to those features that specifically bear upon its lawfulness under the statutes administered by the Commission.

By direction of the Commission.

Staff Memo to the File

June 21, 1977

FROM: Harry Hull

SUBJECT: IWPA Advisory Opinion Request

Today, June 21, 1977, I called Beth Ring, one of the attorneys handling the IWPA request, and asked her to clarify the statement in her March 7 letter that because "there are relatively few suppliers of wire rod, the independent wire producers are greatly dependent on these few sources." She explained that what was meant was that there are few suppliers of wire rod *compared to the number of wire producers* and that independent wire producers, which are not capable of producing their raw material (wire rod), are, of course, dependent upon wire rod suppliers to fill their raw material needs.

Staff Memo to the File

June 20, 1977

FROM: Harry Hull

SUBJECT: IWPA Advisory Opinion Request

I have initiated several phone conversations with Beth Ring and Jack Wasserman about their client's (the IWPA's) advisory opinion request.

June 9, 1977 (Beth Ring). Responding to my inquiry, Ms. Ring informed me that the TSUSA nos. of the wire rods imported by IWPA members were as follows: 608.7000, 608.7100, 608.7300, 608.7500. She also indicated that IWPA members dealt with wire rod suppliers from the following countries—Belgium, Netherlands, U.K., W. Germany, France, and Japan—and that there were more than one supplier for each country. Domestic prices of wire rod are generally higher than foreign, which accounts for the "dependence" of IWPA members on the foreign supply of wire rod, she said. Ms. Ring promised to send some IWPA testimony that might be of some help in understanding the world market for wire rod.

June 10, 1977 (Ring). I asked Ms. Ring to clarify an apparent conflict between a statement in her letter of March 7, (p. 2) which states that "American independent wire producers have been required to purchase wire rod at high, *virtually uniform prices* * * *" (emphasis mine) and a statement in the original request letter (p. 5) which represents that in certain areas of the U.S., independent wire producers appear to pay an unjustifiably higher price for wire rod than such producers in other areas of the country. Ms. Ring explained that in referring to uniformity of prices in her letter of March 7 she meant that wire rod purchasers in a given geographic area of the country were paying virtually identical prices, not that all quotations for rod throughout the U.S. were identical. *June 10, 1977 (Wasserman).* In response to my questions Mr. Wasserman explained that independent wire producers must purchase rod from steel companies that are either "integrated" or "affiliated" with wire producing divisions or companies. This modifies, somewhat, the statement on page 1 of Ms. Ring's March 7 letter to the effect that independents must purchase rod from only *integrated* steel companies.

Mr. Wasserman also estimated that of the domestic wire rod produced, about 50% was sold to independent wire producers and about 50% used by the steel companies producing the rod. [Available statistics give only quantities of wire rod *shipments* and do not reflect total production. See, *e.g.*, AISI Annual Statistical Report, Table 12 (1975); Bureau of the Census, Current Industrial Reports: Steel Mill Products, Table 4 (1975).] He also characterized the wire rod industry as oligopolistic, with 60–70% of total domestic production being supplied by three U.S. companies, and characterized the demand for wire rod as inelastic.

In response to the question of how the export price of foreign wire rod could be relevant to an antidumping proceeding concerning wire or wire products, Mr. Wasserman noted that it was frequently necessary in such proceedings to *construct* the foreign market value of the wire or wire product involved using the export price of foreign wire rod as a starting point. [See 19 U.S.C. § 165.] He said he would send a copy of a recent antidumping complaint concerning upholstery spring wire as an example of how foreign market values are determined in such proceedings.

June 13, 1977 (Wasserman). If foreign wire rod is sold at considerably lower prices to foreign wire producers (integrated, affiliated or even independents), doesn't this explain the lower price of foreign wire and wire products exported to the U.S. as compared to domestic wire and wire products? How, then, can a dumping charge reasonably be made under such circumstances? In answer to these questions Mr. Wasserman pointed out that the difference in price between foreign wire rod sold in this country and abroad does not preclude the possibility of dumping by foreign wire producers. He said that what might appear to be irrational pricing in such dumping contexts was, in economic terms, quite rational. The Japanese, for example, are often content to let their marginal cost equal marginal revenues. Since this discussion was getting over my head he referred me to a white paper by the AISI on Japanese export steel pricing. [I have obtained a copy of that paper from AISI.]

Fourth Supplemental Letter Relative to Request

June 10, 1977

Dear Harry:

Pursuant to your conversation today with Jack Wasserman and myself, I enclose herewith a copy of the 1972 antidumping complaint against upholstery spring wire from Japan.[1]

If you have any further questions do not hesitate to call me at your convenience.

Sincerely,

/s/ Beth C. Ring

Third Supplemental Letter Relative to Request

June 8, 1977

Dear Harry:

Pursuant to our telephone conversation today, I enclose herewith a copy of the presentation made by the Independent Wire Producers Association in December 1976 before the Office of The Special Representative for Trade Negotiations concerning the bilateral agreement between the European Coal and Steel Community and the Japanese Ministry of International Trade limiting exports of Japanese steel to Europe.[1] I refer you specifically to pages 4–14, and to Exhibit 1, which contains the relevant TSUSA numbers for carbon steel wire rod.

Should you have any further questions, please contact me at your earliest convenience.

Sincerely,

/s/ Beth C. Ring

Second Supplemental Letter Relative to Request

May 19, 1977

Dear Harry,

This is to confirm our telephone conversation today concerning the relationship between the Independent Wire Producers Association

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[1] Not reproduced herein.

[1] Not reproduced herein.

("the Association") and the management firm of Smith, Bucklin & Associates, Inc. ("Smith Bucklin"). It was your concern that the closeness of this relationship might jeopardize the anonymity of the member companies in their submitting data to Smith Bucklin pursuant to the proposed reporting system.

Brian Cassedy, an employee of Smith Bucklin, acts as the managing director of the Association. Mr. Cassedy functions as the managing director under authority granted by the Board of Directors of the Association. Since Mr. Cassedy would be under instructions by the Board not to disclose the identity of any reporting member company to any other reporting member company, it would be a violation of his employment and his fiduciary duty to violate such instructions.

Mr. Cassedy has advised me that he will recommend to the Board of Directors that the Association engage the services of Tyson, Belzer & Associates, Inc. to make the statistical compilations and dissemination for the Association. Enclosed herewith is a brochure from Tyson, Belzer & Associates, Inc., which explains the nature of their services and confirms that the information to be reported would be kept on a confidential basis.* This brochure states:

> "It is our policy to work only at the Association level. No consultations are ever provided to individual firms. No information is ever released. *To avoid even accidental data disclosures, many of our analyses contain tight security provision for processing data and presenting results.*" (Emphasis added).

I have also enclosed a description of an example of the type of project conducted to Tyson, Belzer & Associates, Inc.* This description shows that economic and statistical analysis were compiled to form the basis of a presentation before the United States Tariff Commission (now the United States International Trade Commission).

It was very nice meeting you yesterday. Should you have any further questions, do not hesitate to call me at your convenience.

Sincerely,

/s/ Beth C. Ring

First Supplemental Letter Relative to Request

March 7, 1977

Dear Mr. Hull:

I refer to your letter of February 4, 1977, in which you requested additional pertinent information in support of Jack Wasserman's request for confidential treatment of his January 3, 1977 request for an advisory opinion.

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* Not reproduced herein.

Specifically, the "retaliatory action" which Mr. Wasserman mentioned referred to the "dual distribution" nature of the wire producing industry discussed in our Request for an Advisory Opinion. As explained therein, an independent wire producer must purchase its raw material (carbon steel wire rod) from an integrated steel company which produces both wire rod and wire. Thus, the integrated steel companies are suppliers as well as competitors of those companies which purchase the raw material from them. Since there are relatively few suppliers of wire rod, the independent wire producers are greatly dependent on these few sources.

Industry sources indicate that in recent years integrated steel producers located in the European Community, in other European countries and Japan significantly increased the price of wire rod for export to purchasers in the United States. The export prices quoted by these steel producers have been fairly uniform if not identical.

At various times, wire and wire products manufactured in Europe and Japan were imported into the United States at prices substantially below prices which should have prevailed if any reasonable costs of conversion were added to the export price of the rod. Thus, it appears that foreign wire drawers, whether integrated or independent, were acquiring wire rod at prices substantially below the export price of identical wire rod.

Accordingly, American independent wire producers have been required to purchase wire rod at high, virtually uniform prices in order to produce wire and wire products in the United States, but must compete with imported wire and wire products drawn from much lower prices — but identical — wire rod. This, "squeeze" is potentially ruinous to many independent American wire producers.

The Independent Wire Producers Association desires to implement the reporting system on which an advisory opinion was sought. This reporting system would contemplate the dissemination of information among member companies concerning offers received for imported carbon steel wire rod from foreign suppliers. Such an exchange of data would permit documentation of any anti-competitive pricing policies by foreign suppliers, which could then be used in support of one or more actions against such unfair or restrictive trade practices (such as proceedings pursuant to the Antidumping Act of 1921,[1] the Countervailing Duty Law of 1922[2] or the unfair import practice provision).[3] Pursuant to the mandate in Section 337(b)(2) of this latter provision that the United States International Trade Commission should seek advice from the Department of Justice in Section 337 investigations, the Justice Department has recently taken the position that charges filed with the International Trade Commission must be documented with specific evidence:

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[1] 19 U.S.C. §160 *et seq.*

> "* * * the vagueness and non-specificity in the [Welded Stainless Steel Pipe and Tube] complaint does not appear to comply with the Commission's rules requiring 'a statement of the facts constituting the alleged unfair methods of competition and unfair acts,' 19 CFR §210.20(a)(2) and a description of 'specific instances of alleged unlawful importations and sales,' 19 CFR §210.20(A)(3). The broad charges in the complaint * * * unsupported by specific allegations * * * is [sic] not sufficient to meet the tests for a properly specific §337 complaint found in the Commission's rules."[4]

The Association has requested confidential treatment for the FTC's consideration of the proposed reporting system in order to prevent any possible retaliatory action by the foreign suppliers of wire rod in the form of exacerbation of the price squeeze or direct or indirect threats to cut off sources of their raw material (wire rod). Further, since Japanese steel producers each deal through one trading house, they would be very concerned to learn that the American independent producers were discovering the difference or identity between the prices they were quoting to the Americans.

I hope that this information is helpful to you, and if you have any further questions, do not hesitate to call me at you convenience.

Sincerely,

/s/ Beth C. Ring

Staff Letter Relative to Request

February 4, 1977

Dear Ms. Ring:

This is to confirm our telephone conversation of February 3, 1977, in which I requested that your firm provide this office with additional pertinent information in support of Mr. Wasserman's request for confidential treatment of his January 3, 1977, advisory opinion request.

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[2] Tariff Act of 1930, §303, as amended (19 U.S.C. §1303).

[3] Tariff Act of 1930, §337, as amended (19 U.S.C. §1337).

[4] Letter to Hon. Daniel Minchew, Chairman U.S.I.T.C., from Jonathan C. Rose, Deputy Assistant Attorney General, Antitrust Division, Department of Justice (January 25, 1977).

In particular, it is important, in my opinion, that you explain the nature, form, probable extent and impact of the "retaliatory action" which Mr. Wasserman mentioned in his letter as a justification for confidential treatment. In this regard, as I have advised you, there are limits on the Commission's authority to withhold from the public, in whole or in part, agency records—particularly agency "opinions"—under the Freedom of Information Act, 5 U.S.C. 552, and Section 6(f) of the Federal Trade Commission Act, 15 U.S.C. 46(F).

In addition, I requested in our conversation that your firm provide this office with as thorough an explanation as practicable of the use to which the information disseminated to participating members will be put. Such an explanation should include a description of how the information disseminated will alert participating members to "anti-competitive pricing policies" as well as what actions you believe those members are likely to take in the event such "anti-competitive pricing policies" are "discovered". (See page 6 of Mr. Wasserman's advisory opinion request.)

Please feel free to call me if you have any questions about this matter ((202) 523-3496).

Very truly yours,

Harry Hull
Attorney
Office of the General Counsel

Letter of Request

January 3, 1977

Gentlemen:

On behalf of the Independent Wire Producers Association (hereinafter the "Association"), we hereby request, pursuant to Section 1.2, Title 16, Code of Federal Regulation, (19 CFR 1.2), an advisory opinion by the Commission as to the legality under the antitrust laws of a proposed course of action by the Association. The course of action in question (a "raw material reporting system") is not currently being followed and is not the subject of a pending investigation or other proceeding by the Commission or any other governmental agency.

In order to understand the purpose of the proposed course of action to be taken by the Association, it is necessary to explain, briefly, the relatively unusual economic structure of the carbon steel wire producing industry.

The member companies of the Association consist of "independent wire drawers" (defined below). The phrase "wire drawer", describes a company which converts carbon steel wire rod into wire. Wire rod — the raw material — is a steel mill product which is hot rolled from molten slabs of steel ("billets") which are made in giant blast or electric furnaces. Only steel companies with substantial capital assets have the ability to produce the basic steel from which the vital raw material, wire rod, is made.

A wire drawer manufactures wire by "drawing" wire rod through a series of dies. After wire has been produced through this drawing process, the wire is used (either by the wire drawer or other fabricators) to produce thousands of different wire products such as nails, barbed wire, fences, fabric for reinforcing concrete, and hundreds of other products.

Throughout the world, wire drawing companies are described as "integrated", "affiliated" or "independent".

An "integrated" wire drawing company describes a company which has basic steel-making facilities, wire rod rolling facilities and wire drawing facilities.

An "affiliated" wire drawing company does not have the capacity to produce steel or wire rod, but is related directly or indirectly, to an integrated steel company through common ownership or participation in a cartel. Because of the United States antitrust laws, there are few affiliated wire drawing companies located in the United States.

An "independent" wire drawing company has neither steel making capacity, wire rod making capacity nor an affiliation with an integrated steel company. Accordingly, an independent wire drawer must purchase its raw material, wire rod, from steel companies.

Thus, integrated steel companies that produce wire rods and manufacture wire and wire products are — at the same time — suppliers of wire rod as well as competitors of those companies which purchase this raw material from them.*

In light of the above-described nature of this industry, the Association is considering the implementation of an "imported wire rod reporting system," which would consist of the member companies of the Association reporting, on a regular basis, certain information to the statistical branch of a management firm, Smith, Bucklin & Associates, Inc. ("Smith-Bucklin"). Smith-Bucklin has recently entered into an agreement to manage the affairs of the Association.

As contemplated, each member company would be permitted to elect, in its sole discretion, whether or not to report the requested information. A member company which elects to participate would report the following information (on the Form attached hereto as Exhibit A)** concerning each offer it receives for imported carbon steel wire rod:

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* Economists describe an industry where suppliers are also competitors of their customers as a "dual distribution" industry. "Dual distribution" is an uncommon, but recognized economic concept. See "Dual Distribution" in *Report to the President on the Economic Position of the Steel Industry* (Cabinet Committee on Economic Policy, Washington, July 6, 1971) at page 41, containing special mention of the independent wire drawers. Also, see *Dual Distribution*, Hearings Before the Subcommittee on Antitrust and Monopoly of the Senate Committee on the Judiciary, 89th Cong., 1st Sess. (1966); *United States* v. *Aluminum Co. of America*, 148 F.2d, 416 (1945).

(i) the quantity of wire rod offered,

(ii) the foreign country of origin of such wire rods,

(iii) the date on which the offer was received and the date on which the offer was terminated,

(iv) the diameter, carbon content and coil weight of such wire rods,

(v) the calendar quarter of shipment, and

(vi) the f.o.b. (foreign port of exportation) price of the c.i.f. (United States port of importation) price.

The member company reporting this information would not report the name of the offerer or its acceptance or rejection of the offer. Thereafter, Smith-Bucklin would compile such information on an aggregate basis and would reveal neither the names of the specific member companies which supply the information nor the specific prices offered nor the name of the proposed seller. This aggregate information would then be provided on a monthly basis, free of charge, to all member companies of the Association that submitted data for that month.

The Association desires to implement the reporting system in order to survey the pricing policies of foreign steel producers. America's independent wire producers are frequently at a competitive disadvantage in the worldwide markets for wire and wire products because of the "dual distribution" nature of the industry. America's independent wire producers have long suspected (based upon the price of imported wire and wire products) that foreign steel producers have been selling wire rods to related or affiliated foreign wire drawing companies at prices lower than the prices at which they sell similar wire rods to non-related wire drawing companies. Furthermore, in certain areas of the United States where an insufficient amount of wire rod is produced to meet the demand, independent wire producers appear to pay a higher price for wire rod than independent wire producers located in other

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** Not reproduced herein.

areas of the country, without justification and despite the absence of similar price differences between imported wire and wire products.

The Association believes that the dissemination of the information described in the proposed report is necessary to enable the member companies to act in the event of anti-competitive pricing policies by foreign suppliers.

We would appreciate the Commission's opinion concerning the legality of the proposed reporting system. Should you require further information, please do not hesitate to contact us.

Respectfully,

/s/ Jack Gumpert Wasserman

Lawfulness under the antitrust laws administered by the FTC of a voluntary Code of Advertising Standards proposed by the Wine Institute, File 783 7006.

Opinion Letter

March 31, 1978

Dear Mr. DeLuca:

This is in response to your letters of September 23 and October 11, 1977, requesting an advisory opinion regarding the lawfulness under the laws administered by the Commission of a voluntary Code of Advertising Standards proposed by the Wine Institute. The Wine Institute is a trade association of the California wine industry representing wineries accounting, in 1976, for more than half of all wines sold in the United States. You have stated that the purpose of the Code is to encourage advertising reflecting the industry's concern with maximum social responsibility and high standards in wine advertising. You also request Commission advice regarding proposed circulation of the Code by the Institute, if approved, to nonmember wineries and other wine associations for their information and solicitation of various media organizations for their adoption of a code embodying the principles contained in the subject Code of Advertising Standards.

The Commission understands that adherence to the Code by the wine producer members of the Institute will be completely voluntary. Individual members will determine for themselves whether to comply with the Code and whether their advertising conforms to its requirements. No sanctions will be imposed, directly or indirectly, for noncompliance with the Code's provisions. The Institute has given assurances to the Commission that its by-laws concerning suspension, expulsion or termination of membership or the imposition of fines and penalties, have no application to voluntary compliance or noncompliance with the proposed advertising Code. The Code does not apply to wholesalers or retailers of wine products and, as represented, is nondiscriminatory among wine producers insofar as limitations upon advertising opportunities are concerned.

The Commission has not considered, and therefore expresses no opinion regarding, the ethical concerns addressed by the Code. Accordingly, the advice rendered by the Commission pertains solely to the propriety of the proposed actions under the antitrust laws.

In the Commission's view, the antitrust laws do not prevent a completely voluntary forbearance by industry members from the use of advertising themes perceived as socially undesirable, so long as no undue restraint of trade ensues. The Wine Institute's objective of encouraging the promotion of wine products by domestic wine producers in a socially responsible manner may well be laudable. Particular care must be taken, however, to assure that limitations on advertising, even voluntary ones, do not operate anticompetitively or in such manner as unreasonably to restrict competitive alternatives or foreclose competitors in any market.

In addition to reviewing the submitted proposal to assure that effective competition in the domestic wine industry not be adversely effected, the Commission has considered possible downstream consequences, as well, of Code provisions that could secondarily operate to limit particular media markets or the commercial opportunities of persons associated with affected aspects of media advertising. To assure that limitations of this nature are minimized, the Institute has informed the Commission that the Code will be amended to eliminate a specific age designation for show models and personalities by omitting the words "are or" from Guideline 4(a), as well as in Guideline 4(c) to add the words "children's or juveniles' " before "magazines."

The Commission has decided it should interpose no objection to presentation of the proposed Code by the Wine Institute to its members. This decision is based on the Institute's assurance that no coercion, direct or indirect, will attend the decision by any member as to whether it will or will not comply with the provisions of the Code, the Code's clearly noncommercial purposes and the limited nature of secondary restrictive effects on persons or entities engaged in businesses allied to advertising or to wine distribution and sale. The Commission, however, maintains the right to withdraw its approval in accordance with § 1.3(b) of the Rules of Practice in the event implementation of the Code results in coercion or competitive foreclosure or should the public interest otherwise so require.

In view of the foregoing considerations, the Commission has decided to reserve opinion at this time concerning overtures to nonmember wine producers to adopt the Code, including unsolicited initial contacts with specific nonmembers for such purpose. A basic qualification to the Commission's affirmative opinion regarding presentation of the Code by the Wine Institute to its members is that the Code be completely voluntary. Nonmembers of the Institute will be free to communicate interest in the Code if they so desire and the Code will undoubtedly receive sufficient publicity to enable their doing so.

A special problem is presented by the Institute's proposal to request media organizations to adopt parallel advertising guidelines. Such activity on the part of the Wine Institute, if fully successful, could as a practical matter render compliance with the Code's provisions compulsory rather than voluntary from an individual wine producer's perspective. Because pressures in this direction possess a significant potential for coercively inducing modifications in the advertising practices of competitors that could be commercially advantageous to those responsible for formulation of the Code, Commission approval cannot be extended to this aspect of the proposal.

By direction of the Commission.

Supplemental Letter Relative to Request

October 11, 1977

Dear Mr. Garvey:

In connection with our request of September 23, for an advisory opinion, we are hereby requesting a Commission opinion rather than a Staff opinion.

We wish to stress that there is no application of the provisions of Article VII, Section 6, of the Wine Institute By-Laws relating to "Suspension, Expulsion and Termination of Membership" to this proposed voluntary Wine Institute Code of Advertising Standards.

I am enclosing a newly revised proposed voluntary Wine Institute Code of Advertising Standards which makes clear that "These guidelines shall apply only to the voluntary subscribers to this Code of Advertising Standards".[1]

This revised document should be considered by the Commission in lieu of the version submitted with our letter of September 23.

Thank you for your interest.

Sincerely,
WINE INSTITUTE

By
/s/ Arthur H. Silverman
Washington Counsel

Letter of Request

September 23, 1977

Dear Mr. Thomas:

Pursuant to 16 CFR 1.1 *et. seq.*, I am requesting an informal advisory opinion whether the attached proposed voluntary Wine Institute Code of Advertising Standards violates any statutes, rules or regulations administered by the Federal Trade Commission.* The proposed Code will not be adopted until receipt of a favorable Federal Trade Commision informal advisory opinion. To our knowledge, we are not the subject of a pending investigation or proceeding by the Federal Trade Commission or any other federal or state government agency.

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[1] Not reproduced herein.

Wine Institute, the non-profit trade association of the California wine industry, represents 240 wineries whose members account for approximately 91% of the wineries in California. In 1976 Wine Institute members accounted for 72.5% of total California wine shipments. California, in turn, produced about 71.6% of the wine sold in the United States, while other states produced 12.7%. Imports accounted for 15.7% of the American wine market.

The proposed Code of Advertising Standards would apply to the advertising of all wines produced by member wineries. Thus, in addition to grape table wine, the advertising of dessert wines, flavored wines, sparkling wines, wines produced from fruit other than grapes, and all other wines would be subject to the Code.

The proposed course of action involves a program that is totally voluntary and carries no sanctions whatsoever against any member not in compliance. Each winery would determine if its own advertising is in conformity with the Code, and whether it desires to follow the Code. There are no enforcement provisions.

We believe the proposed Code to be absent of anti-competitive features at both the vertical and horizontal levels.

The Code does not refer to, nor would it apply to, wholesalers or retailers. There are thus no problems at the vertical level.

Similarly, at the horizontal level, the Code contains no provisions which could in any way imply price fixing, territorial allocation, or any other prohibited areas. In fact, there is no provision for any agreement among any member wineries as to whether they would (or would not) comply with the Code. In addition, we can discern no elimination of competitive prerogatives in other ways, such as if the provisions of the Code applied in an obviously restrictive manner to certain types of producers while innocuous to most.

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* Not reproduced herein.

Moreover, we cannot foresee any possible discrimination in advertising opportunities.

We ask that the Commission advise us on the substance of the Code and assure us that it is satisfactory in that it includes no anti-competitive measures.

With regard to the substance of the proposed Code, please advise us on the following:

> Do we address ourselves to the issues and types of concerns of interest to the Federal Trade Commission in wine advertising?

With regard to the non anti-competitive area, please advise us on the following:

1. May the members of Wine Institute agree to this totally voluntary Code which carries no sanctions whatsoever?
2. After approval by the members of Wine Institute, would it be a violation of the statutes, rules and regulations administered by the Federal Trade Commission to submit the Code to non-member wineries and other wine associations for their information?
3. After approval of the Code by the members of Wine Institute would it be a violation of the statutes, rules and regulations administered by the Federal Trade Commission to request various organizations, such as the National Association of Broadcasters, to adopt a code embodying the principles contained in the proposed Wine Institute Code of Standards?

I would appreciate acknowledgement of the receipt of this request.

Thank you for your interest.

Very truly,
/s/ John A. De Luca
President

Compliance advisory opinion as to whether nine proposed advertisements* if published, would comply with the order issued on March 16, 1970 (77 F.T.C. 277), Dkt. 8792.

Opinion Letter

April 20, 1978

Dear Mr. Lamberson:

This is in response to your letters of July 25, 1977, September 2, 1977 and September 8, 1977, on behalf of your clients, Golden Fifty Pharmaceutical Co., Inc., and Michael Posen requesting an advisory opinion as to whether nine proposed advertisements comply with an order of the Commission issued on June 29, 1970 [sic]. The requests were made pursuant to Section 3.61(d) of the Commission's Rules of Practice.

This is to advise you that the Commission has determined that none of the nine proposed advertisements, if published, would comply with the 1970 order.

The nine proposed advertisements are identified as follows:

Submission Number	*Date Submitted*	*Product Line*	*Identified by You as*
1	7/25/77	Golden Fifty	(unnumbered)
2	9/2/77	Golden Fifty	Exhibit A
3	9/2/77	Cosmetique	Exhibit B (COS-01)
4	9/2/77	Cosmetique	Exhibit C (COS-02)
5	9/2/77	Cosemtique	Exhibit D (COS-03)
6	9/2/77	Cosmetique	Exhibit E (COS-04)
7	9/2/77	Cosmetique	Exhibit F (COS-05)
8	9/8/77	Golden Fifty	GF-02
9	9/8/77	Golden Fifty	GF-03

Paragraph 1(b) of the Commission's order prohibits your clients from "Disseminating or causing the dissemination of . . .any advertisement which: . . .(b) Represents directly or by implication that any product is offered free or under any other terms when the offer is used as a means of enrolling those who accept the offer in a plan whereby additional supplies of the product are shipped at an additional charge *unless all of the conditions of the plan are disclosed clearly and conspicuously and within close proximity to the "free" or other offer."* (emphasis added)

At the bottom of Submission 1 there is a coupon which includes the statement: "I may cancel at any time by sending in the cancellation card included with each shipment." The top part of the advertisement which contains the "$3.00 Bottle of Vitamins Free" offer makes no mention of the cancellation card requirement. It is the opinion of the Commission that the failure to disclose the cancellation card requirement in close proximity to the free offer would constitute a violation of Paragraph 1(b).

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* Not reproduced herein.

Each of Submissions 2 through 7 are designed to be folded in thirds. When folded each of them contain a "free" or other offer on the cover. None of them adequately disclose the full conditions of the monthly or bi-monthly program on the cover. Instead, a prospective customer would have to open the advertisements and read the conditions either in the body of the advertisements or on the attached reply coupon. It is the Commissions opinion that the failure to disclose all of the conditions of the plan on the cover of Submissions 2 through 7 in close proximity to the "free" or other offer would be a violation of Paragraph 1(b) of the order.

The Commission also believes that the conditions disclosed in Submission 2 are contradictory and unclear in violation of Paragraph 1(b) and may also violate Paragraph 1(c). The letter included in the top of Submission 2 implies that the customer has an option to decide in advance whether he wants additional supplies of Golden Fifty tabulets. The coupon implies that additional supplies will be sent automatically. This contradiction violates Paragraph 1(b) in that the conditions of the plan are not clearly disclosed and may also violate Paragraph 1(c) which prohibits any representation that an offer is made without obligation when in fact there is an obligation to receive additional monthly supplies.

Submission 2 also fails to explain what is meant by the "10-day approval" language which appears solely in the coupon and not in close proximity to the free offer on the cover or on the middle of the page above the coupon. Furthermore, the "I may cancel at any time. . ." language in the coupon is confusing when compared to the "10-day approval" language. These failures would be a violation of Paragraphs 1(b) and 1(c) and may also be a violation of Paragraph 1(d) which prohibits an offer for a limited period of time unless such limitations are actually imposed.

The Commission is also of the view that the conditions of the plan utilized in Submission 3 are unclear and confusing in violation of Paragraph 1(b). It is not clear from the language in this proposal whether the special annual "$100 Prestige Perfume Collection," if accepted by the consumer counts towards the four kits that need to be purchased over the next two years. The cover and body of Submission 3 and the coupon attached to the proposal make the representation that the "$74 Beauty Kit for Only $1" is yours if you join the club *and* agree to buy four kits over the next two years. The Commission is of the opinion that unless the proposal adequately discloses what is the penalty for failing to buy four kits, it is not in compliance with Paragraph 1(b).

The reply coupons in Submissions through 7 use the term "on approval" and also state "I may return any kit for full credit (or refund)" without any limitations. Unless the advertisement clearly explains what is meant by "on approval" it does not comply with Paragraph 1(b). The Commission also notes that the return privilege (Cosmetique pays postage) is not set out on the cover or in the body of the flyer above the reply coupon in close proximity to the offer. This may constitute anotne: failure to comply with Paragraph 1(b).

The reply coupons in Submissions 3 through 7 contain the limitation that only one introductory kit is offered per household; that the offer is void if previously accepted; and that the offer is good only in the USA. It is the Commission's view that these limitations are conditions of the plan and in order to comply with Paragraph 1(b) should be set out on the cover and in the body of the ad in close proximity to the offer.

Submissions 3 through 7 each contain photographs of various identifiable cosmetic items. In order to comply with Paragraph 1(f) of the order, the Commission is of the opinion that the "$74 Beauty Kit for Only $1" sent to customers must contain these identifiable items. The advertisements also contain representations that customers receive "full-size" cosmetics, "*never* any samples." It is not possible to determine from the photographs if the cosmetic items so displayed are full size and not samples. Therefore, the Commission is of the opinion, that the advertisements would violate Paragraph 1(g) of the order if the photographed items and the items actually included in your client's kits are less than regular commercial size or are "trial" or "sample" size.

Submissions 6, 7, 8 and 9 all use the term "trial membership" yet there is no explanation as to whether a trial membership differs from a regular membership. In order to comply with Paragraph 1(b), the Commission is of the opinion that the conditions of the trial membership should be disclosed clearly and conspicuously and within close proximity to the free or other offer. Continued use of the term, without explanation, would be confusing and a violation of Paragraph 1(b).

The top and back of Submissions 8 and 9 contain the "$3.00 Bottle of Vitamins Free" offer followed by the conditions of the plan. Both advertisements contain "Dear Friend" letters explaining that additional monthly supplies will be shipped automatically. The Commission is of the view that the conditions mentioned on the top and back fail to disclose the automatic aspect of the monthly shipments. This could cause confusion in the minds of some customers and would therefore be a violation of Paragraph 1(b).

Finally, the Commission advises you that the opinion expressed herein apply solely to the question as to whether the nine proposed advertisements comply with the Order of the Commission issued June 29, 1970. The Commission has made no determination concerning the legality of any other representations, contained in the proposed advertisements, which do not come within the terms of the order, Docket 8792. In taking this action, the Commission has not considered the various advertisements which have been submitted to the Commission's staff pursuant to the Court's Injunction of June 6, 1977.

By direction of the Commission.

Second Supplemental Letter Relative to Request

September 8, 1977

Dear Sir:

On behalf of our clients, Golden Fifty Pharmaceutical Co., Inc. and Michael A. Posen, we are herewith requesting, pursuant to §3.61(d) of Subpart G of Part 3 of Subchapter A of Chapter 1 of the 16th Volume of the Code of Federal Regulations, advice from the Federal Trade Commission as to whether a proposed course of action, if pursued by our clients, will constitute compliance with an outstanding Commission Cease and Desist Order.

On June 29, 1970, the Federal Trade Commission issued an Order, FTC Docket No. 8792, against our clients, pursuant to the provisions of Section 5 of the Federal Trade Commission Act, prohibiting the continued use of certain methods and forms of advertising. In order to secure continued compliance with this Order, our clients herewith submit two (2) advertisements of Golden Fifty Pharmaceutical Co., Inc. (marked Exhibits GF-02 and GF-03) intended for publication in the near future. We would ask the Commission to kindly consider the proposed advertisements and inform our clients whether or not the advertisements, if published, would comply with the Order.

Should the Commission need additional information concerning either the proposed advertisements or their distribution, please do not hesitate to contact us, for our clients wish to fully cooperate with the Commission in order to prevent future difficulties of any kind.

It should be noted that this request for an advisory opinion is in addition to, and not in place of, the two prior requests submitted by us on July 25, 1977 and September 2, 1977.

Very truly yours,

CHAPMAN AND CUTLER

By
/s/ Harry P. Lamberson

First Supplemental Letter Relative to Request

September 2, 1977

Dear Sir:

On behalf of our clients, Golden Fifty Pharmaceutical Co., Inc. and Michael A. Posen, we are herewith requesting, pursuant to §3.61(d) of Subpart G of Part 3 of Subchapter A of Chapter 1 of the 16th Volume of the Code of Federal Regulations, advice from the Federal Trade Commission as to whether a proposed course of action, if pursued by our clients, will constitute compliance with an outstanding Commission Cease and Desist Order.

On June 29, 1970, the Federal Trade Commission issued an Order, FTC Docket No. 8792, against our clients, pursuant to the provisions of Section 5 of the Federal Trade Commission Act, prohibiting the continued use of certain methods and forms of advertising. In order to secure continued compliance with this Order, our clients herewith submit one (1) advertisement of Golden Fifty Pharmaceutical Co., Inc. (marked Exhibit A) and five (5) advertisements of Cosmetique Beauty Club, Inc. (marked Exhibits B, C, D, E and F) intended for publication in the near future. We would ask the Commission to kindly consider the proposed advertisements and inform our clients whether or not the advertisements, if published, would comply with the Order.

Should the Commission need additional information concerning either the proposed advertisements or their distribution, please do not hesitate to contact us, for our clients wish to fully cooperate with the Commission in order to prevent future difficulties of any kind.

It should be noted that this request for an advisory opinion is in addition to, and not in place of, the request submitted by us on July 25, 1977. We understand that our request of July 25, 1977 has been referred to the Federal Trade Commission Regional Office in Chicago, Illinois, and our clients await the Commission's response to this earlier request.

Very truly yours,

CHAPMAN AND CUTLER
By
/s/ Harry P. Lamberson

Letter of Request

July 25, 1977

Dear Sir:

On behalf of our clients, Golden Fifty Pharmaceutical Co., Inc. and Michael A. Posen, we are herewith requesting, pursuant to §3.61(d) of Subpart G of Part 3 of Subchapter A of Chapter 1 of the 16th Volume of the Code of Federal Regulations, advice from the Federal Trade Commission as to whether a proposed course of action, if pursued by our clients, will constitute compliance with an outstanding Commission Cease and Desist Order.

On June 29, 1970, the Federal Trade Commission issued an Order, FTC Docket No. 8792, against our clients, pursuant to the provisions of Section 5 of the Federal Trade Commission Act, prohibiting the continued use of certain methods and forms of advertising. In order to secure continued compliance with this Order, our clients herewith submit an advertisement of Golden Fifty Pharmaceutical Co., Inc. intended for publication in the near future. We would ask the Commission to kindly consider this proposed advertisement, and inform our clients whether or not the advertisement, if published, would comply with the Order.

Should the Commission need additional information concerning either the proposed advertisement or its distribution, please do not hesitate to contact us, for our clients wish to fully cooperate with the Commission in order to prevent future difficulties of any kind.

We eagerly await the Commission's response.

Very truly yours,

CHAPMAN AND CUTLER

By
/s/ Harry P. Lamberson

Development and sale of market data to marketers of food products would not violate order of June 1, 1961 (58 F.T.C 977), modified, 307 F.2d 184, Dkt. 6459.

Opinion Letter

May 1, 1978

Dear Mr. Solomon:

The Commission has considered your request for advice as to whether Giant Food Inc. ("Giant") may engage in a proposed course of conduct whereby Giant would develop market data for business entities engaged in the marketing of food products without violating the order issued by the Commisson on June 1, 1961.

By order of the Commission, 58 F.T.C. 977 (1961), *modified*, 307 F.2d 184 (D.C. Cir. 1962), Giant may not knowingly induce and receive discriminatory display or promotional allowances. Giant proposes to collect and disseminate market data collected through use of computer assisted checkout systems. Giant intends to contract with marketers of products, including its own suppliers, for preparation of this data. You state that the availability of this service would not be conditioned on the contracting party's status as a Giant supplier, and that Giant will not induce any party to purchase the market data.

On the basis of the facts submitted, you are advised that the Commission is of the opinion that the offer and sale of the market data would not violate the Commission's order in Docket No. 6459. We would advise you that any attempt by Giant to condition its patronage with suppliers upon their purchase of the information service might well constitute as illegal and anticompetitive trade practice.

The above advice in no way affects a given supplier's or seller's responsibility to adhere to the requirements of the Robinson-Patman Act, or to Giant's responsibility to adhere to the provisions of the order in its dealings with any of its suppliers.

By direction of the Commission.

Letter of Request

December 2, 1977

Dear Mr. Thomas:

This petition is filed pursuant to Section 3.61(d) of the Commission's Rules of Practice which provides that any respondent subject to a Commission order may request advice from the Commission as to whether a proposed course of action, if pursued by it, will constitute compliance with such order.

Giant Food Inc., hereinafter referred to as Giant, is giving serious consideration to a proposal which involves the sale of its services to various parties and seeks timely advice from the Commission to insure that its actions will not contravene the provisions of the Cease and Desist Order.

The Commission issued a complaint against Giant on November 21, 1955 charging a violation of Section 5 of the FTC Act, as amended. The Commission's decision issued on June 1, 1961 required Giant to cease soliciting and accepting as compensation for advertising and promotional services, discriminatory payments from its suppliers which it knew, or should have known, were not made available on proportionally equal terms to all its competitors in connection with an "anniversary sale" (58 FTC 977).

The decision of the Commission was affirmed by the United States Court of Appeals for the District of Columbia on June 14, 1962 (307 F.2d 184). In affirming the decision of the Commission, however, the Court of Appeals stated that "The order should be directed toward prohibition of a knowing inducement and receipt of, or contracting for, the receipt of discriminatory display and promotional allowances." Thus, the Court of Appeals limited the order and the scope to the general practices involved in the complaint.

In recent years, Giant has developed extremely sophisticated and technical information which could be of great value to persons engaged in the marketing of food products. This information is collected from Giant's computer assisted checkout systems and permits it to develop data on a given product and anticipate trends as to shelf-space allocation, advertising or special sales. Data can be retrieved from each store so equipped and the movement on any item can be analyzed. In addition, reports can be generated for a given brand, including comparisons, with the movements of similar or competitive products. Projections can be made as to the frequency at which products will be ordered and the frequency of movements from a variety of designated positions on the shelf can be studied. Further, Giant has the capability of conducting spot tests by studying the pattern of placement and handling of products and in this manner report on the effects of juggling either location, number of products, placement in other departments to determine the best sales position. In short, the capabilities of Giant in this regard permit a number of variables and the information can be generated if a determination is made to expend the funds necessary to retrieve the information.

Many marketers of products, including Giant suppliers, are familiar with the unique capabilities that Giant possesses to produce information of this kind. This information is of proven value. Giant is being asked to produce the information and has been offered payment to cover its expenses and anticipates some profit in this regard. Because this may involve, in some instances, the receipt of funds from suppliers who are presently selling merchandise to Giant, even though not connected with purchase or resale, the program raises a question as to the applicability of the Order to Cease and Desist.

We believe that the present Cease and Desist Order does not inhibit the practice of producing and selling information sought by parties in those instances where the parties involved may also happen to be a supplier. Giant does not intend to induce anyone to purchase information but will, to the extent of its capacity, develop information for anyone including present suppliers or their competitors who do not sell to Giant. The Robinson-Patman Act does not prohibit any and every transaction no matter how remote between a customer and a supplier, and we believe the course of action proposed will not contravene the provisions of the order. . . .

We solicit the advice of the Commission and urge that the request be processed as soon as possible because Giant is postponing its decision to pursue this course of action until it hears from the Commission.

Sincerely,

/s/ Lawrence P. Solomon

Proposed establishment of a program for certifying individuals who fit prescription footwear (pedorthists), and facilities which provide pedorthic services, File 783 7008.

Opinion Letter

June 15, 1978

Dear Mr. Krill:

This is in response to your request for an advisory opinion concerning a certification program proposed by the Board for Certification in Pedorthics (BCP). After considering your request, the Commission has determined that it cannot approve the program.

According to your submission, the BCP proposes establishment of a program for certifying individuals who fit prescription footwear (pedorthists) and facilities which provide pedorthic services. Certified individuals would be required to fulfill certain continuing education obligations, pay an annual fee, and adhere to a code of ethical professional conduct. Facilities would be certified upon a demonstration that they meet certain minimum requirements.

The Commission recognizes that certification programs can be helpful to consumers by informing them that practitioners (and establishments) meet meaningful levels of occupational competency. All such programs, however, must be carefully structured and implemented so that (1) consumers are not misled or unfairly affected, (2) potential entry restraints are held to a minimum; and (3) competition is not otherwise unreasonably restricted. The Commission is of the opinion that several facets of the BCP program fail these tests.

First, the requirements for qualification of applicants are too indefinite, and the purpose of certain standards for facility certification are too uncertain. For example, the requirements that an applicant have had "sufficient" clinical experience and that a facility maintain "adequate" staff and have a "professional" appearance are too subjective and could lead to arbitrary limitations on certification.

Second, although an appeal process is available to rejected applicants, to facilities denied certification and to other aggrieved parties, ultimate decisions are made by the same Board which was responsible for initial adverse decisions. Moreover, although the composition of the governing Board of Directors would include directors nominated by outside organizations, such as an orthopedic medical group, a majority would consist of Prescription Footwear Association members, who are competitors of candidates for certification.

Third, certified pedorthists would be subject to unreasonable "ethical" obligations, imposed by "Canons of Ethical Conduct" and promulgated by the Prescription Footwear Association. These provisions impose significantly increased potential for unfair or anticompetitive practices. The Canons can be construed to impose, for example, prohibitions against advertising the availability and prices of pedorthic services. This is couched in terms of distinguishing between so-called "professional" and "commercial" aspects of pedorthic practice.

The Canons forbid, as well, open criticism of the services provided by a competitor. All fee sharing, presumably for shared servicing, is also unreasonably prohibited. No disclosed commercial or ethical justification for these restrictions appears.

The Commission, for each of the reasons noted herein, cannot advise the BCP that its proposed certification plan is acceptable. In summary, the Commission believes that no certification program should be so structured that competing practitioners can determine who is or is not to be certified, based upon subjective, undefined criteria. Nor can the Commission approve a plan which permits ultimate certification decisions to be made, even in part, by persons not distinct and separate from the initial certification decision-makers. Finally, there is no place in such a program for rules, codes, or understandings the effect of which are to place unreasonable limitations upon effective competition.

By direction of the Commission.

Letter of Request

June 17, 1976

Dear Mr. Lewis:

On May 31, 1973 Mr. Thomas J. Segal, Attorney, Office of General Counsel commented on a proposed certification program for the fitters of prescription footwear. This letter of comment followed a request on behalf of the Prescription Footwear Association that the pending request for an advisory opinion be held in abeyance, pending certain revisions of the proposed program. At this time, we wish to bring you up to date regarding the development of this program and to reinstate our request for advisory opinion or, in lieu thereof, additional staff comments, regarding this certification process.

We believe that we have met or exceeded all requirements made known to us in correspondence, such as Mr. Segal's letter, and staff conferences. More recently, we sought additional staff advice by means of a conference with Mr. Ben Burman of your office. As a result of that conference, certain additional changes were made in the organizational structure of the entity which will conduct the certification program for individuals and for facilities.

What has transpired since our initial submissions is that a separation has occurred between the trade association of prescription shoefitters and the credentialing organization. The trade association, formerly an Indiana corporation, has been reorganized and has become a non-profit corporation under the laws of the District of Columbia. Copies of the merger and the reorganization agreement which achieved this restatement of the trade association's character are attached. In connection with this statutory merger, the By-laws of the P.F.A. were amended; these are also appended to this letter.

For the last several years, the Prescription Footwear Association has concentrated on publications for the purpose of informing its members and on the conduct of educational seminars to improve their skills, background and scientific understanding of the fitting of prescription footwear. Examples are attached hereto.

On October 4, 1974 the Board for Certification in Pedorthics, Inc. had its first organizational meeting of its Board of Directors. At that time, the program to initially certify an individual as a "Certified Pedorthist" (C.Ped.) was developed. At that time modifications were approved, amending the criteria for certification to conform to Mr. Segal's recommendations:

a) The five-year experience requirement for certification as a Pedorthist has been eliminated.

b) The educational prerequisites for certification as a Pedorthist have been eliminated.

c) The inventory requirements for Facility Accreditation have been reviewed, modified and substantiated as to cost and reasonableness.

d) Due process safeguards, including opportunities for a fair hearing, have been incorporated throughout the Individual and Facility Certification program.

Every effort has been made to insure that this credentialing program will have as its sole purpose the provision of a reasonable level of assurance to orthopaedic surgeons and other prescribers of prescription footwear that prescriptions will be filled with a degree of skill and accuracy which is adequate to provide the necessary service to the patient on an effective and efficient basis. This is the whole point of the credentialing program. It is not to restrict the numbers of persons authorized to fill prescriptions for footwear, but on the other hand, it is a response to a need expressed by the Foot Society of the American Academy of Orthopaedic Surgeons.

In most areas of the United States a prescription for footwear for a diabetic, rheumatoid, arthritic, injured, deformed or insensitive foot could be filled by a supermarket. This certification program does not purport to offer absolute assurance that each holder of the certified status will provide skilled and knowledgeable services on each and every occasion. But it is a distinct improvement over the completely unpredictable situation in prior years.

We would be pleased to discuss this matter at an informal conference arranged at your offices. Should you require additional information, that would be supplied promptly.

In the event that you wish to provide us with information concerning the activities of credentialing and professional organizations and societies, particularly in view of your recent activities in connection with the American Medical Association, would you kindly forward such information to us.

Thank you sincerely for your cooperation in this matter. Please let me know if there is anything further that I might do to facilitate your consideration of this program.

Very truly yours,

/s/ Edward J. Krill

Magnuson-Moss Warranty Act—Interpretation of Section 102(b) of the Act, 15 U.S.C. 2302(h), and the Commission's Rule on Pre-Sale Availability of Written Warranty Terms, 16 CFR 702, as they apply to certain situations that arise in the home building industry; and the applicability of Section 111(d) of the Act, 15 U.S.C. 2311(d), to a warranty required on all FHA/VA financed housing, File 783 7009, 43 F.R. 35684.

Opinion Letter

June 21, 1978

Dear Mr. Colton:

This is in reply to your request of September 28, 1977, on behalf of the National Association of Home Builders, for an advisory opinion concerning Sections 102(b) and 111(d) of the Magnuson-Moss Warranty Act, 15 U.S.C. 2301, *et seq.*, and the Commission's rule on the Pre-Sale Availability of Written Warranty Terms, 16 C.F.R. 702, as they apply to the home building industry.

Your request contains five topics of discussion, each posing questions for Commission consideration. The Commission has rephrased your request in eight questions in order to clarify the issues posed. It has determined that the rephrased questions numbered 1 through 3 (below) are not appropriate for an advisory opinion under Part 1, Subpart A of the Commission's Rules of Practice; instead these questions are treated as a request for an exemption from Rule 702, 16 C.F.R. 702. Where the Commission has granted an exemption from Rule 702, that exemption applies to all affected home builders and wholesale suppliers.

The rephrased questions and the Commission's answers are as follows:

1. When a builder gives the purchaser an allowance to select various fixtures or appliances (consumer products) from a third party supplier, is it the builder or the third party supplier who must comply with the pre-sale availability of warranties requirements for "sellers" under 16 C.F.R. 702.3(a) in each of the following situations:

    (a) The purchaser makes selections from stock purchased wholesale by, and in the possession of, the builder, and makes payment to the builder for any items selected in excess of the allowance.

    (b) The purchaser makes selections in the showroom of the builder's supplier, from items not yet purchased by the builder, and makes payment to the builder for any items selected in excess of the allowance.

(c) The purchaser makes selections from items not yet purchased by the builder, and makes payment directly to the supplier for any items selected in excess of the allowance.

2. What are a custom builder's duties as a "seller" under 16 C.F.R. 702 when the purchaser can choose from among virtually all brands of appliances available in the marketplace?

3. If the builder has made the pre-sale warranty information available to the purchaser for all appliances from which the purchaser can choose, does the builder have any obligation under 16 C.F.R. 702 to make warranty information available, after a contract is signed, for substitute appliances which the purchaser must select due to a manufacturer's discontinuation or replacement of the appliance initially chosen by the purchaser?

4. Does the Magnuson-Moss Warranty Act require that all builders' warranties contain a clause assigning the manufacturers' warranties on consumer products to the purchaser, or does the Act have the effect of automatically making all manufacturers' warranties on such appliances run to the ultimate purchaser?

5. Is the builder or the purchaser the proper party to complete and return the warranty registration cards for consumer products installed in the home?

6. Does Section 111(d) exempt the mandatory FHA/VA warranty from the requirements of the Magnuson-Moss Warranty Act?

7. Is a builder who gives only the mandatory FHA/VA warranty required to comply with 16 C.F.R. 702 for those consumer products sold with warranties that are covered by the Act?

8. If a builder both gives the mandatory FHA/VA warranty, and voluntarily offers an additional warranty not required by any Federal law (e.g., a one year warranty against defects in materials and workmanship), to what extent is the additional warranty subject to the Magnuson-Moss Warranty Act?

The Commission has carefully considered the matters set forth in your letter. It is the Commission's determination that:

1. (a) When a builder gives a purchaser an allowance to select consumer products, and the purchaser makes selections directly from the builder's stock, the builder *must* comply with the seller's duties under 16 C.F.R. 702.3(a) to make warranty terms available prior to sale.

(b) & (c) When a builder gives a purchaser an allowance to select consumer products from the stock of the builder's supplier, the builder is exempted from compliance with 16 C.F.R. 702.3(a). In this latter situation, the builder's supplier is also not required to comply with the seller's pre-sale duties under the rule if the supplier's sales are totally wholesale, including builder-referred sales.

2. When a purchaser contracts to have a custom home built, and pursuant to the contract can choose appliances from among virtually all of those available in the marketplace, the builder is exempted from compliance with the seller's duties under 16 C.F.R. 702.3(a) to make the text of written warranties available prior to sale.

3. A builder must make warranty terms available for inspection by a purchaser if, after a contract is signed, the purchaser must make a second selection because originally selected items have become unavailable. The builder is not exempted from compliance with 16 C.F.R. 702.3(a) in this situation.

4. The Magnuson-Moss Warranty Act does not govern the issue of whether a manufacturer's warranty on a consumer product must be assigned by a builder to the home purchaser. This question is governed by state law.

5. Registration cards would be prohibited for all full warranties under the Commission's rule on Reasonable Duties Under a Full Warranty, as proposed in 43 F.R. 39223 (August 3, 1977); see also the Commission's Interpretations of the Act, 16 C.F.R. 700.7(b). However, registration cards are permitted for limited warranties. When a limited warranty offered on a consumer product by a manufacturer includes the registration card, the home purchaser is the proper party to complete and return the card, unless the warranty specifically requires this of retailers.

6. Section 111(d) of the Magnuson-Moss Warranty Act exempts the mandatory FHA/VA warranty offered by a builder from the requirements of the Act (except for Section 102(c)).

7. A builder who gives only a FHA/VA warranty must still make available under 16 C.F.R. 702 those warranties that are covered by the Act; the fact that the FHA/VA warranty is generally exempt from the Act does not affect the builder's status as a "seller" of consumer products covered by warranties that are governed by the Act.

8. Any warranty offered by a builder on a consume product that is not required by Federal law is subject to the provisions of the Magnuson-Moss Warranty Act.

By direction of the Commission.

1208

Letter of Request

September 28, 1977

Dear Mr. Thomas:

This firm represents the National Association of Home Builders of the United States (NAHB). On behalf of that organization and pursuant to Part I, subpart A of the Commission's Rules of Practice, we hereby request an advisory opinion on the following questions relating to the application of Title I of the Magnuson-Moss Act to the home building industry.

The Commission will no doubt recall that it, NAHB and Home Owners Warranty Corporation have had extensive discussions over the last several years concerning the difficulty of applying to the building industry a statute which was drafted with an eye to the customary retail consumer transaction where both the product and the details of the transaction are far less complicated than are a new dwelling and its transfer. NAHB sponsored several seminars in various parts of the country to inform and educate builders about the Act and to discuss questions arising from the nature of dwelling sales. These questions were repeadedly asked; none of those present, including representatives of our industry who have intensively studied the Act, and observers from the Commission, were certain of the answers.

I. FIXTURE AND APPLIANCE ALLOWANCES

It is a common practice in the home building industry for the purchaser of a new home to request and to be granted an allowance for the purchase of appliances, light fixtures, carpeting, and/or other items, some of which might be considered consumer products. Under this practice, the purchaser is permitted to select (either from stock in the builder's possession or at the warehouse of showroom of the builder's supplier of such items) up to a certain dollar amount of specified items. The builder will install the selected items (in substitution for similar items normally provided) in the home with no addition to the purchase price. If the purchaser selects items costing more than the allowed dollar amount, the purchaser must pay the difference.

For example, the purchaser of a $50,000 home might be given a $300 allowance for light fixtures of purchaser's selection. The builder would direct the purchaser to the showroom of the builder's electrical supplier. If the purchaser selected $400 worth of light fixtures at the showroom, the builder would install them in the home provided that (depending upon the arrangement between the builder and the supplier) (a) the purchaser paid $100 (the excess over the allowance) to the supplier at the time he made his selections or (b) the purchaser paid $50,100 for the house, so that the builder could pay the additional $100 to the supplier.

The specific question is the application to such a practice of Section 102(b) of the Act and Part 702 of the Commission's Regulations. Under an allowance arrangement such as that outlined above, is it the builder or his supplier who must maintain copies of warranties on consumer products which can be selected by the purchaser under each of the following circumstances:

1. The purchaser makes his selections from stock purchased wholesale by, and in the possession of, the builder, and makes payment to the builder for any items selected in excess of the allowance.
2. The purchaser makes his selections at the showroom of the builder's supplier, from items not yet purchased by the builder, and makes payment to the builder for any excess (with the builder in turn paying the supplier).
3. The purchaser makes his selections in the showroom of the builder's supplier from items not yet purchased by the builder, and makes payments direct to the supplier for any excess (the builder, of course, paying the supplier the amount of the allowance).

In our view, presale availability of these warranties in situations 2 and 3 should be the responsibility of the supplier rather than the builder because it is at the supplier's facility that the consumer compares the available items and makes his selections, and it is there that he should have the opportunity to compare the written warranties on those items as well. The fact that in situation number 2 the title to the items may technically have passed to the builder does not alter the fact that the convenience of the consumer is best served, and the comparison shopping intended by the Act's drafters is most strongly stimulated, if the presale display of written warranties takes place at the supplier's facility.

II. CUSTOM BUILDER

In contrast to the usual consumer product transaction where the purchaser buys an already completed item from the stock of a retailer, or (as in the case of an automobile) orders an item from a catalog and selects from among a limited number of available options, many new homes are constructed on a truly custom basis according to the purchaser's specifications (which may be either general in nature or a complete design prepared by the purchaser's own architect), generally on land already owned by the purchaser. In such custom building transactions, the selection of brand and model of appliances is not made until long after the construction contract has been signed and construction is under way – in the context of a $50,000 to $100,000 transaction involving countless decisions as to structural materials, configuration of rooms, interior decor, etc., the choice between two brands of dishwashers does not loom large. In addition, in such a situation, the purchaser's choice is not among a few brands or models maintained in inventory by the builder or provided by those suppliers with whom the builder has a continuing relationship. The builder will generally obtain and install whatever appliance the purchaser asks for, and the purchaser's choice is among virtually all the appliances available in the marketplace.

It should be noted that this is a selection which the purchaser may in fact be reluctant to make prior to signing the contract, (a) because of its comparative unimportance in the context of the much larger construction transaction and (b) because he may want to wait until late in the construction process, when the final cost of the home can accurately be estimated, before selecting the types (and hence the cost) of appliances to be installed.

Advice is requested as to the following question: What, if anything, must the custom builder do under Part 702 of the Commission's Regulations when the question of the type, brand and model of appliances does not arise until construction is under way pursuant to a binding construction contract? In our opinion, it is impossible for the custom builder to have available the written warranties on all the consumer products from which his purchaser might choose, because, since the custom builder does not maintain an inventory of appliances or equipment but rather procures on an *ad hoc* basis whatever his customer requests, the alternatives (and hence the number of warranties that would have to be placed in a binder and kept up to date) number in the hundreds or thousands.

III. NECESSARY SUBSTITUTION

Another common practice in the industry is for the purchaser to view a model home and sign a contract with the builder for the purchase of a lot on which, by the time of closing, the builder will have constructed a home similar to the model. In such a situation, because the builder is constructing a number of similar homes, the purchaser has available either (a) only a single brand of appliances which the builder offers or (b) a selection, allowed by the builder, among two or three equivalent, alternative brands and models. The appropriate time for installation of the appliances selected by the purchaser will not arrive until the dwelling is nearly completed, several months after the purchaser has made his selection and the binding contract has been signed. By that time, one or more of the models selected by the purchaser may either have been discontinued by the manufacturer or been replaced by a more recent model having different features.

Advice is requested as to the following question: If in the above situation the builder has (in compliance with Part 702) maintained available, for inspection by the purchaser before he signs the contract, the warranties on those appliances from which the purchaser was invited to make his selection, does the builder have any obligation under Part 702 with regard to availability of warranties on substitute appliances which the purchaser must select because of the discontinuance or replacement of the chosen appliance by the manufacturer?

IV. WARRANTY REGISTRATION CARDS

Prior to the advent of the Magnuson-Moss Act, there was some question as to whether manufacturers' warranties on appliances which were installed in new homes ran to the builder or to the ultimate purchaser of the home. To deal with this problem, the builder's warranty frequently contained a clause formally assigning benefits of those warranties to the purchaser, and the builder delivered to the purchaser at closing, for completion by the purchaser, whatever warranty registration cards the appliance manufacturers required to be completed and submitted to the manufacturer as a precondition to warranty effectiveness.

Advice is requested as to the following two questions:

1. Does the Magnuson-Moss Act require that all builders' warranties contain such an assignment clause, or does it have the effect of automatically making all manufacturers' warranties on such appliances run to the ultimate purchaser?
2. Who is the proper party to complete such warranty registration cards and send them to the manufacturer?

V. VA/FHA WARRANTY

Both the Veterans Administration and the Federal Housing Administration (a part of the Department of Housing and Urban Development) require, as a condition to their guaranty or insurance of the purchaser's mortgage on any new dwelling, that the seller of the dwelling (the builder) warrant in writing that it has been constructed in substantial conformity with the plans and specifications which were used by the agency as the basis for its determination that the dwelling was of sufficient value to constitute adequate security for it and the lender. For your information, a copy of the standard form suggested by these agencies for this warranty is attached to this letter as Exhibit A.

Section 111(d) of the Act provides that (with one exception) Title I does not apply to whatever portion of a written warranty is governed by federal law. Advice is requested as to the following questions:

1. Are the form and content of the mandatory FHA/VA warranty exempt from the requirements of the Act?

2. If a builder gives a written warranty consisting of two parts, one of which is the mandatory FHA/VA warranty language while the other is an additional warranty not required by either agency (e.g., a one-year warranty against defects in materials and workmanship), to what extent are its form and content subject to Title I of the Act?

3. Is a builder who gives only the mandatory FHA/VA written warranty required to maintain copies of manufacturers' warranties on appliances and equipment available for inspection by purchasers before they sign binding contracts to purchase homes?

In our opinion, these questions provide a further illustration of the difficulty of regulating new home warranties and the home purchase transaction in the same way as more conventional retail transaction in purely personal property. We would appreciate the Commission's advice and assistance in furnishing definitive answers to these questions.

Very truly yours,
COLTON AND BOYKIN

/s/ Herbert S. Colton

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